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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

October Term, ~~1937~~ 8

No. ~~860~~ 11

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

ROBERT C. WINMILL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED MARCH 12, 1938
CERTIORARI GRANTED APRIL 11, 1938

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 860

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

ROBERT C. WINMILL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX

64448—38——1

1 Before United States Board of Tax Appeals

Docket No. 79,036

Robert C. Winmill, petitioner
v.
Commissioner of Internal Revenue, respondent

Docket entries

Appearances:
For Taxpayer: Thomas M. Wilkins, Esq., William E. Hayes, Esq.
For Commissioner: John H. Pigg, Esq.

1935

Apr. 10—Petition received and filed. Taxpayer notified. (Fee paid.)
Apr. 11—Copy of petition served on General Counsel.
Apr. 27—Answer filed by General Counsel.
May 6—Copy of answer served on taxpayer.
May 8—Notice of appearance of Thomas M. Wilkins as counsel filed.
Sept. 9—Hearing set October 28, 1935.
Oct. 16—Motion to place on the Circuit Calendar for hearing in vicinity of New York City filed by taxpayer. October 18, 1935, granted.

1936

Mar. 5—Hearing set May 12, 1936, at New York, New York.
May 12—Hearing had before Mr. Mellott on merits. Submitted. Stipulation of facts as filed be admitted in evidence. Stipulation of facts filed. Briefs due as per rules.
2 June 2—Transcript of hearing of May 12, 1936, filed.
July 17—Motion for leave to file brief, brief lodged, filed by taxpayer. July 18, 1936, granted.
July 20—Copy of motion and brief served on General Counsel.
July 25—Memorandum brief filed by General Counsel.
Aug. 31—Reply to memorandum brief filed by taxpayer. September 1, 1936, copy served.

1937

Mar. 31—Opinion rendered, Arthur J. Mellott, Division 11. Judgment will be entered under Rule 50.
Apr. 5—Motion to vacate decision and reconsider issues filed by taxpayer. April 12, 1937, denied.
Apr. 20—Motion to grant a rehearing and reconsider opinion filed by taxpayer. Brief in support of motion attached April 26, 1937, denied.
Apr. 28—Notice of settlement filed by General Counsel.
Apr. 30—Consent to settlement filed by taxpayer.
May 3—Decision entered, Arthur J. Mellott, Division 11.

May 28—Motion to fix amount of bond in the amount of $7,750.00 filed by taxpayer.
May 28—Order fixing amount of bond at $7,750.00 entered.
June 30—Supersedeas bond in the amount of $7,750.00 approved and ordered filed.
3 July 6—Petition for review by United States Circuit Court of Appeals (Second) with assignments of error filed by taxpayer.
July 6—Proof of service filed by taxpayer.
July 15—Agreed statement of evidence lodged.
July 15—Praecipe filed by taxpayer.
July 15—Proof of service of praecipe filed.
July 15—Agreed statement of evidence approved and ordered filed.

Before United States Board of Tax Appeals

[Title omitted.]

Petition

Filed April 10, 1935

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his deficiency notice (Bureau symbols IT: AR: A-2-LHA-90D) dated January 14, 1935, and as a basis of his proceeding alleges as follows:

4 1. The petitioner is an individual with his place of business at 1 Wall Street, New York, New York.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on January 14, 1935.

3. The taxes in controversy are Federal income taxes for the calendar year 1932. The deficiency asserted is $5,508.14, the entire amount of which is in controversy.

4. The following assignments of error are alleged by the petitioner to have been committed by the Commissioner in determining said deficiency:

"(a) Failure of the Commissioner to allow as a deduction, losses in the amount of $8,473.06 sustained by this petitioner through the partnership of Gude, Winmill & Co. in the sale of stocks and bonds during the taxable year which were held by the petitioner for less than two years.

"(b) Failure of the Commissioner to offset against the petitioner's income from sales of stocks and bonds during the taxable year, which were held by him for less than two years, through the partnership of Gude, Winmill & Co. of which petitioner was a member during the taxable year, losses in an equal amount, namely, $8,473.06, sustained by the petitioner from the sale during the taxable year of stocks and bonds held by him for less than two years.

5 "(c) The disallowance by the Commissioner of losses sustained by the petitioner during the taxable year in the amount of $2,247.65 on the sale of stocks and bonds held by him for less than two years.

"(d) The failure of the Commissioner to offset losses of the petitioner in the amount of $2,247.65 sustained during the taxable year from the sale of stocks and bonds which were held by the petitioner for less than two years against gains in an equal amount, namely, $2,247.65, from the sale by the petitioner during the taxable year of stocks and bonds held by him for less than two years in joint account in which the petitioner had a direct fractional interest.

"(e) The disallowance by the Commissioner of commissions paid or incurred during the taxable year in carrying on the petitioner's trade or business in the amount of $19,045.25.

"(f) Failure of the Commissioner to allow as a deduction during the taxable year, commissions in the amount of $19,045.25 paid by the petitioner during the taxable year in carrying on the petitioner's trade or business.

"(g) The disallowance by the Commissioner of stock losses in the amount of $172,771.02.

"(h) Failure of the Commissioner to allow as a deduction during the taxable year, stock losses in the amount of $172,771.02."

6 5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

"(a) During the calendar year 1932 petitioner actively carried on the business of speculating, trading or dealing in stocks and other securities. Practically all of the petitioner's time devoted to his business affairs was spent in speculating, trading or dealing in stocks and bonds. During the taxable year the petitioner's losses from sales or exchanges of stocks and bonds held by the petitioner for less than two years exceeded the gains from such sales or exchanges during the taxable year by $162,050.31. Included in such gains of the petitioner during the taxable year 1932 were gains in the amount of $8,473.06, which said gains were derived through the sale by the petitioner during the calendar year 1932 of stocks and bonds which had been held by the petitioner for less than two years, through the partnership of Gude, Winmill & Co., 1 Wall Street, New York, New York. Included in such gains of the petitioner during the taxable year 1932 from the sale of stocks and bonds held by him for less than two years are gains in the amount of $2,247.65 which gains were derived from the sale by the petitioner during the year 1932 of stocks and bonds which were held by the petitioner for less than two years in certain joint accounts in which the petitioner held a direct fractional interest during all of the calendar year 1932. The joint ac-

count designation and the interests of the petitioner in the
7 gains from the sale in such accounts during the calendar year 1932 of stocks and bonds held for less than two years, are set forth below:

"W. H. Short a/c		$501.25
"R. C. Winmill	#825 a/c	146.56
"	#33-1 a/c	360.27
"	#33-2 a/c	1,239.57
		$2,247.65

"(b) The Commissioner of Internal Revenue in determining the deficiency erroneously refused to apply the gains of the petitioner from the sales during the taxable year of stocks and bonds held for less than two years in the amount of $8,473.06 against losses from such sales incurred by the petitioner during the same year on the ground that the gains in the said amount of $8,473.06 were the gains of the partnership of Gude, Winmill & Co. and, hence, were not the gains of this petitioner. On this ground the Commissioner erroneously added to the income of this petitioner for the calendar year 1932 $8,473.06.

"(c) The Commissioner of Internal Revenue in determining the deficiency of this petitioner refused to apply against the losses of this petitioner from the sales of stocks and bonds held less than two years, the amount of $2,247.65 representing the gain derived by this petitioner from the sale of stocks and bonds held for less than
8 two years directly through joint accounts. The Commissioner, therefore, erroneously added to the income of this petitioner for the calendar year 1932 $2,247.65 on the erroneous ground that this income, although derived by the petitioner from the sale of stocks and bonds held by him less than two years, cannot be offset against the petitioner's losses on sales of stocks and bonds held less than two years in a different joint account or as an offset against the petitioner's losses otherwise sustained from the sale of stocks and bonds held for less than two years.

"(d) In computing the limitation on stock losses under Section 23 (r) of the Revenue Act of 1932 the Commissioner erroneously computed the excess of losses from sales or exchanges of stocks and bonds over the gains from such sales or exchanges during the taxable year 1932 as $172,771.02, instead of only $162,050.31. The difference between these two sums, namely, $10,720.71, is made up of (a) the $8,473.06 item representing the excess of gains of the petitioner derived through the partnership of Gude, Winmill & Co. of which the petitioner was a member, from sales of stocks and bonds held less than two years over losses sustained from sales of stocks and bonds held less than two years, and (b) the $2,247.65 representing the excess of gains of this petitioner derived through joint accounts from the sale of stocks and bonds held by the petitioner for less than two years over losses sustained from sales of stocks and bonds held less than two years.

9 "(e) During the calendar year 1932 the petitioner was actively engaged in the carrying on of a trade or business, namely, that of speculating, trading or dealing in stocks and bonds. Practically all of the petitioner's time devoted to his business affairs was spent in the conduct of such trade or business. During the calendar year 1932 in the course of the conduct of such trade or business the petitioner made 816 purchases and sales of stocks and/or bonds. These transactions involved purchases of 64,517 shares and involved the sale of a like number of shares, 64,517 shares. These said shares of stock were purchased for a total cost of $2,961,254.95 and were sold for $2,781,533.99. On these purchases and sales so made during the calendar year 1932 by the petitioner in the conduct of the said trade or business, the petitioner paid brokerage commissions in the amount of $19,045.25. The total buying and selling commissions paid by this petitioner in connection with the 816 trades completed by the petitioner during the calendar year 1932 on the said purchase and sale of 64,517 shares of stock above referred to totaled $19,224.75. This amount represents the buying commissions on securities long on January 1, 1932 which were sold during the year 1932, plus the selling commissions thereon and the buying and selling commissions on securities which were bought and sold during the year 1932. The commissions on securities bought and held over the end of the

10 year 1932 are not included. The purchase commissions on securities long January 1, 1932 in the petitioner's various accounts amounted to $602.50 (this amount is included in the $19,244.75 item). The purchase commissions on securities long December 31, 1932 in the petitioner's various accounts amounted to $403.00 (this amount is not included in the $19,244.75).

"(f) In computing the said deficiency the Commissioner erroneously added to the cost of shares sold by the petitioner during the calendar year 1932, commissions in the amount of $19,224.75. Thus, by adding commissions to the cost of stock sold during the calendar year 1932 and by erroneously disallowing $172,771.02 of the loss sustained, the Commissioner erroneously disallowed in excess of $17,000.00 of the said $19,224.75 commissions paid or incurred during the calendar year 1932 in the course of petitioner's trade or business of speculating, trading or dealing in stocks during the said year."

6. Wherefore, the petitioner prays that this Board may hear the proceeding and determine that there is no deficiency due from the petitioner for the calendar year 1932.

(Signed) Thomas M. Wilkins.
THOMAS M. WILKINS.
(Signed) William E. Hayes,
WILLIAM E. HAYES,
Counsel for Petitioner,
602 Shoreham Building, Washington, D. C.

11 [*Duly sworn to by Robert C. Winmill; jurat omitted in printing.*]

Exhibit A to petition

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, Jan. 14, 1935.

Mr. ROBERT C. WINMILL,
% Gude, Winmill, and Company,
1 Wall Street, New York, New York.

SIR: You are advised that the determination of your income tax liability for the year(s) 1932 discloses a deficiency of $5,508.14 as shown in the statement attached.

12 In accordance with section 272 (a) of the Revenue Act of 1932, as amended by section 501 of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT: C: P-7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
By (signed) CHAS. T. RUSSELL,
Deputy Commissioner.

Enclosures: Statement. Form 870.

13 STATEMENT

IT: AR: A-2.
LHA-90D.

In re: Mr. Robert C. Winmill, % Gude, Winmill and Company, 1 Wall Street, New York, New York

Income Tax Liability Year 1932; Income Tax Liability $5,508.14; Income Tax Assessed, None; Deficiency $5,508.14.

The deficiency shown herein is based upon the report dated June 29, 1934, prepared by Revenue Agent John A. O'Brien, and transmitted to you under date of September 25, 1934, which report has been reviewed and approved by this office.

The principal issue involved is whether losses from sales of securities held less than two years may be applied against other income,

and profit derived through joint trading accounts. This loss has been disallowed as a deduction by this office, inasmuch as the Revenue Act of 1932 does not contain any provision whereby losses on sales of stock held less than two years may be applied against other income or offset income from joint trading accounts in securities.

A synopsis of your adjusted income tax liability follows:

14 Income shown on return (loss)		$136,546.44
Add: Partnership income (decrease)		8,473.06
Total (loss)		$145,019.50
Add:		
Stock profit joint accounts	$2,247.65	
Stock losses	172,771.02	175,018.67
Adjusted income		$29,999.17
Add: Capital net loss		22,560.05
Income subject to surtax		52,559.22
Less:		
Dividends	$11,785.00	
Personal exemption	4,100.00	15,885.00
Income subject to normal tax		$36,674.22
Normal tax at 4% on $4,000.00		$160.00
Normal tax at 8% on $32,674.22		2,613.94
Surtax on $52,559.22		5,554.21
Total		$8,328.15
Less: 12½% of capital net loss of $22,560.05		2,820.01
Total tax assessable		5,508.14
Tax previously assessed		None
Additional tax to be assessed		$5,508.14

15. In accordance with telephone instruction of your representative under date of December 31, 1934, the formal notice of deficiency is now being issued.

A copy of this letter, together with a copy of the statement, has been mailed to your representative, William E. Hayes, Little Building, Boston, Massachusetts, in accordance with the authority conferred upon him in the power of attorney executed by you and on file with the Bureau.

Before United States Board of Tax Appeals

[Title omitted.]

Answer

Filed April 27, 1935

The Commissioner of Internal Revenue, by his attorney, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, in answer to the petition of the above-named taxpayer, admits and denies as follows:

1. Admits that the petitioner is an individual with place of business at 1 Wall Street, New York, New York.

16 2. Admits that a notice of deficiency was mailed to the petitioner on January 14, 1935, and that a true and correct copy of said notice of deficiency is attached to the petition.

3. Admits that the taxes in controversy are Federal income taxes for the calendar year 1932, but denies that the amount in controversy is correctly stated in paragraph 3 of the petition.

4. (a) to (h), inclusive. Denies that the Commissioner of Internal Revenue erred in manner and form as alleged in subparagraphs (a) to (h), inclusive, of paragraph 4 of the petition.

5. (a) to (f), inclusive. Denies all the allegations of fact as set forth in subparagraphs (a) to (f), inclusive, of paragraph 5 of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that petitioner's appeal be denied.

(Signed) Robert H. Jackson,
Assistant General Counsel for the Bureau of Internal Revenue.

Of Counsel:
E. L. Corbin,
Special Attorney, Bureau of Internal Revenue.
ELC-GA 4-26-35.

17 Before United States Board of Tax Appeals

Docket No. 79,036

Robert C. Winmill, petitioner,
v.
Commissioner of Internal Revenue, respondent

Opinion

Promulgated March 31, 1937

Taxpayer, a member of a partnership engaged in the stock brokerage business, operated three securities trading accounts as an individual and also operated four accounts jointly with others. During the taxable year he reported a gain from his partnership interest and from the operation of the joint accounts and a large loss from the operation of his individual accounts. All of the securities sold were noncapital assets. In computing the amount of the loss and gain on these accounts, buying commissions were included as part of the cost and selling commissions as an offset against the selling price. Held:

"(1) Section 23 (r) of the Revenue Act of 1932, limiting the amount of losses on the sale of noncapital assets to the gains from the sale of such assets, is constitutional.

"(2) Taxpayer's gains from the partnership and from the joint accounts can not be offset against the losses sustained on his individual accounts.

18 "(3) Commissions paid to brokers in buying and selling securities are not deductible either as ordinary and necessary business expenses or as losses sustained. Commissions paid in purchasing securities are a part of the cost and those paid in selling securities are an offset against the selling price."

Thomas M. Wilkins, Esq., for the Petitioner. John H. Pigg, Esq., for the Respondent.

MELLOTT: Petitioner seeks redetermination of a deficiency in income tax for the calendar year 1932 in the amount of $5,508.14. In his income tax return for said year he reported as income and claimed as deductions items as follows:

INCOME

Line 3. Interest on Bank Deposits, Notes, Corporation Bonds, etc. (except interest on tax-free covenant bonds)	$29,876.34	
Line 5. Income from partnerships, Syndicates, Pools, etc. Gude-Winmill & Co., No. 1 Wall Street, New York, New York	27,984.15	
Line 8. Loss on Sale of Stocks, Bonds, etc. (From Schedule C) In connection with business		$172,771.02
Line 10. Dividends on: (a) Stock of Domestic Corporations subject to taxation under Title I of 1932 Act	$11,785.00	
Line 12. Deficit in Items 1 to 11		$103,125.53

19 DEDUCTIONS

Line 14. Taxes paid (Explain in Schedule F)	10,860.86	
Line 18. Other Deductions not Reported above (Explain in Schedule F) Capital loss held over 2 years	22,560.05	
Line 19. Total Deductions in Items 13 to 18		33,420.91
Line 20. Net Loss (Item 12 plus Item 19)		136,546.44
Line 22. Net Deficit for Tax Computation		136,546.44

At the hearing before us the following facts were stipulated:

"(1) During the calendar year 1932 and for several years prior thereto the petitioner, Robert C. Winmill, was a member of the partnership of Gude, Winmill & Co., with offices at No. 1 Wall Street, New York, New York, which said partnership was engaged in the stock brokerage business.

"(2) During 1932 petitioner operated three separate securities trading accounts the entire interest in each of which was his own. During that year he sold 61,992 shares of stock through said three accounts in 419 separate sales transactions representing stock purchases of 61,992 shares made through the said three accounts in 353 separate

purchases, the cost of which to the petitioner was $2,884,531.14,
20 exclusive of purchase commissions, which amounted to $8,911.00. Of these commissions $1,417.50 were paid by petitioner in 1931 and $7,493.50 were paid by petitioner in 1932. The said 61,992 shares of stock were sold in 1932 by petitioner for $2,722,904.37. During 1932 petitioner paid brokers commissions on said sales in the amount of $9,574.00. During 1932 petitioner also paid sales taxes on said sales in the amount of $5,072.95.

"(3) During 1932 petitioner operated jointly with other persons four securities trading accounts in each of which he had a fractional interest, and which accounts were operated as joint ventures. Each of these accounts was operated at a profit. During that year there were sold 2,525 shares of stock through said four accounts in 22 separate sales transactions representing stock purchases of 2,525 shares made through the said three accounts in 22 separate purchases. Petitioner's share in the cost of the said 2,525 shares of stock was $68,300.00. Petitioner's share of the buying commissions paid by him on said purchases during 1932 amounted to an additional $270.00. The said 2,525 shares of stock were sold through the said four accounts during 1932 for an amount of which petitioner's share was $71,687.88. Petitioner's share of the selling commissions paid by him during 1932 amounted to $273.75. Petitioner's share of the sales taxes paid by him during 1932 on said sales amounted to $66.83. Petitioner's
21 share of the gains from these said four joint accounts during 1932 amounted to $2,267.80, after payment of all costs and expenses.

"(4) None of the shares sold through any of the above described seven accounts was held for two years or more.

"(5) On his 1932 return petitioner claimed a loss deduction of $172,771.02, on account of the 419 sales transactions and the 22 sales transactions described in paragraphs (2) and (3), above. In his determination of the deficiency involved, the Commissioner disallowed the deduction so claimed on the petitioner's return, and increased the petitioner's income for the year 1932 by the following amounts:

"Stock profit joint accounts	$2,247.65
"Stock losses	172,771.02
"Total	$175,018.67

"(6) The taxes above referred to in the amount of $5,072.95 were claimed as a deduction by petitioner in his 1932 return and were allowed by the Commissioner.

"(7) At the end of the year 1932 petitioner had on hand in his said three individual trading accounts, shares of stock on which commissions in the amount of $403.00 were paid by him in 1932, which is not included in any of the amounts of commissions hereinabove described and set forth.

"(8) No part of the broker's commissions, above referred to, in the amounts of $8,911.00, $9,574.00, and $403.00 have been allowed by the Commissioner as deductions.

22 "(9) Except as to broker's commissions, as shown herein above, the petitioner kept his records and filed his returns, including his records and return for the year 1932, on the cash receipts and disbursements basis."

Petitioner's and respondent's joint exhibit A-1 shows in detail the result of the operations of the seven trading accounts. It discloses a total loss on the sales made through the three individual accounts in the amount of $175,038.82, said amount including commissions but not tax (the taxes having been claimed and allowed as deductions). It shows also the petitioner's share of the net gain from the operations of the four joint stock trading accounts in which he had an interest and which accounts were operated as joint ventures, such distributive share of the net gain being $2,267.80.

In addition to the stipulated facts petitioner testified, and we find as a fact, that he devoted a portion of his time to the operation of the seven trading accounts.

The controversy between the parties is chiefly because the respondent applied section 23 (r) of the Revenue Act of 1932[1]
23 and disallowed, as a deduction from petitioner's gross income, the losses sustained by him in the several trading accounts. Upon brief, petitioner argues that the section is unconstitutional and void. The pleadings apparently raise no such issue and perhaps it should not be considered. Frederick N. Dillon, 20 B. T. A. 690; Coca-Cola Bottling Co., 22 B. T. A. 686. But inasmuch as the section merely places a limitation upon the deduction of losses, we are satisfied that it is constitutional. "Unquestionably, Congress has power to condition, limit, or deny deductions from gross income in order to arrive at the net that it chooses to tax." Burnet v. Thompson Oil & Gas Co., 283 U. S. 301, 304. Stanton v. Baltic Mining Co., 240 U. S. 103; Brushaber v. Union Pacific Railroad Co., 240 U. S. 1, 23, 24. Helvering v. Independent Life Insurance Co., 292 U. S. 371-381; Commissioner v. Lafayette Life Insurance Co., 67 Fed. (2d) 209; Lloyd v. Commissioner, 55 Fed. (2d) 842. Any doubt which may have existed as to the constitutionality of the section is completely dispelled by the opinion of the Court of Appeals for the Second Circuit in the recent case of Davis v. United States, — Fed. (2d) — (Jan. 4, 1937). Nothing more need be said on this point.

Section 23 (r) being constitutional and valid, may petitioner offset his gains from the partnership of Gude, Winmill & Co. and from the four joint accounts by his losses on the three accounts owned and operated by him individually? We think not.

---

[1] (r) LIMITATION ON STOCK LOSSES.—

(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

(2) Losses disallowed as a deduction by paragraph (1), computed without regard to any losses sustained during the preceding taxable year, shall, to an amount not in excess of the taxpayer's net income for the taxable year, be considered for the purposes of this title as losses sustained in the succeeding taxable year from sales or exchanges of stocks or bonds which are not capital assets.

Section 1111 (a) (3) of the Revenue Act of 1932 defines "partnership" as follows:

"(3) The term 'partnership' includes a syndicate, group,
24 pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this Act, a trust or estate or a corporation; and the term 'partner' includes a member in such a syndicate, group, pool, joint venture, or organization."

It is clear that if petitioner and his associates were not partners in the generally accepted sense of the term, they were nevertheless engaged in a joint venture in conducting the four joint accounts and dividing the profits and losses, and, at least for present purposes, such joint ventures must be considered as partnerships. This brings us, then, to the question decided in Percy H. Johnston, 34 B. T. A. 276. It was there held that a partner, entitled as such to a share of the profits of a partnership upon its sale of non-capital assets, could not in computing his individual taxable income, reduce his share of profits therefrom by the amount of his loss upon the sale of similar assets owned by him individually. Our decision was recently (December 7, 1936) affirmed by the Circuit Court of Appeals for the Second Circuit (Johnston v. Commissioner, — Fed. (2d) —). The court in its opinion says: "* * * the petitioner must treat his share of the partnership gain as ordinary income in his return since he cannot sustain the claimed right to have it retain there its status as a gain derived from the sale of non-capital assets, by bringing it within one of the exceptions to the general rule which Con-
25 gress has created." This conclusion was reached upon a consideration by the court of the various sections of the revenue act relating to partnerships, which, the court said, disclosed a scheme providing, "in general for the carrying over into his own return of a partner's distributive share of partnership income as computed in the partnership information return as so much ordinary income without noticing its source as shown by the partnership return except in those instances for which especial provision has been made." (Johnston v. Commissioner, supra.) We accordingly hold that the proposed offset can not be made.

The remaining contention of petitioner is that even if section 23 (r) is constitutional and applicable, nevertheless the commissions paid to brokers in connection with the buying and selling of speculative securities are deductible from gross income either as ordinary and necessary business expenses under the provisions of section 23 (a) of the Revenue Act of 1932, or as losses, under the provisions of section 23 (e) of the same act.

All of the revenue acts have allowed, as deductions from gross income, the ordinary and necessary expenses of carrying on a trade or business and losses incurred in trade or business or in transactions entered into for profit; but commissions paid in purchasing and selling speculative securities have never been held to be deductible either as business expenses or as losses. Prior to 1932, the Treasury regulations

consistently provided that commissions paid in purchasing securities are a part of the cost price of such securities and commissions paid in selling securities are an offset against the selling price.
26 Par. 108, Regulations 33 (Revised) (1916); art. 293, Regulations 45 (1918); art. 293, Regulations 62 (1921); art. 292, Regulations 65 (1924); art. 292, Regulations 69 (1926); and art. 282, Regulations 74 (1928). This regulation has been upheld by the courts and by this Board in a number of decisions. E. P. Greenwood, 34 B. T. A. 1209; Florence G. Baldwin, 23 B. T. A. 512; I. N. Burman, 23 B. T. A. 639; Frank Cavanaugh, 19 B. T. A. 1251; and Hutton v. Commissioner, 39 Fed. (2d) 459, affirming 12 B. T. A. 265.

In Hutton v. Commissioner, supra, the Circuit Court of Appeals for the Fifth Circuit said:

"It is clear that the taxpayer suffers no hardship by the rule, as the commission paid in purchasing the securities may be deducted from the profits or added to the losses when the securities are eventually sold."

The regulation was tacitly approved by the Supreme Court in Helvering v. Union Pacific Railroad Co., 293 U. S. 282. In that case the Court, holding that commissions paid by a taxpayer for the sale of its own bonds were not deductible as ordinary and necessary expenses, said:

"In this respect the commissions do not differ from brokerage commissions paid upon the purchase or sale of property. The regulations have consistently treated such commissions, not as items of current expense but as additions to the cost of the property or deductions from the proceeds of sale, in arriving at net capital profit or loss for purposes of computing the tax."

27 Does section 23 (r) require a modification of, or a departure from, the consistent treatment which has always been accorded to brokerage commissions paid upon the purchase or sale of speculative securities? We think not. The section merely places a limitation upon the deductions from gross income which may be taken as "losses from sales or exchanges" of noncapital assets by providing that they "shall be allowed only to the extent of the gains from such sales or exchanges."

Petitioner argues that if Congress had intended to include commissions within such losses, it would have made specific reference to them either in section 23 (r) or in section 23 (t). He refers to the familiar rule enunciated by the Supreme Court in Gould v. Gould, 245 U. S. 151, and oft applied by this Board, that tax levying statutes are not to be extended by implication and doubt is to be resolved in favor of the taxpayer. But the rule is not applicable here. Congress did not define "losses" and we must presume that the term was used in the section in question as it had been construed by the courts and by this Board. "Unless the contrary appears, statutory words are presumed to be used in their ordinary and usual sense, and with the meaning commonly attributable to them." DeGanay v. Lederer, 250 U. S. 376.

But, says petitioner, unless the commissions are allowed as ordinary and necessary business expenses or as losses they will never be reflected againt taxable income in any year. We do not agree with this contention. The effect of adding the commissions to the cost of the
28 stock purchased in 1932 and offsetting them against the selling price of the stock sold in that year was to increase the amount of the losses for that year. Under the provisions of section 23 (r) (2) losses, disallowed as a deduction by paragraph (1) of the same section, to an amount not in excess of the taxpayer's net income for the taxable year, were to be considered for the purpose of computing his income as losses sustained in the succeeding taxable year from sales or exchanges of stocks or bonds which were not capital assets. Such losses, under the construction of the Department, approved by the courts and by this Board, included the commissions. It is clear that if petitioner had sufficient gains from the sale of noncapital assets in 1933 to absorb the losses disallowed in 1932, he suffered no hardship by the treatment accorded to the commissions. The mere fact, if it is a fact, that he did not have sufficient gains in 1933 to enable him to so utilize all of the 1932 losses, does not justify overturning or setting aside the rule theretofore consistently followed by the Department for the computation of such losses.

The regulation as amended in 1932 has not been considered by the courts or by this Board. So far as pertinent herein it reads:

"Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in selling securities when such commissions are not an ordinary and necessary business expense, are an offset against the selling price. [Art. 282, Regulations 77.]

The italicized portion was added in 1932.

29 Petitioner contends that the regulation as amended authorizes the deduction of the selling commissions from the gross income of a trader in securities as ordinary and necessary expenses of carrying on a trade or business. Having reached this conclusion he takes the next step and contends that if the selling commissions are deductible then no good reason exists for treating otherwise the buying commissions. But did the amendment to the regulations have such a far-reaching effect? We think not. A clue to what was intended by it may be gleaned from a memorandum of the general counsel of the Department issued about the time that it was made. Therein (G. C. M. 15430, XIV-2 C. B. 59) it is stated, in effect, that the Department had undertaken, by the amendment in question, to create an exception to the general rule, which was to be applicable only to dealers in securities. We need not decide whether such exception was valid or not, nor do we pass upon it. But we do decide that the amendment did not have the effect of making the brokerage commissions, paid by a trader in securities, deductible either as ordinary and necessary expenses of carrying on a trade or business or as losses.

It follows that the deficiency determined by the respondent should be, and it is, approved.

Reviewed by the Board.

Judgment will be entered under Rule 50.

SMITH and DISNEY concur only in the result.

30 *Dissenting opinion*

ARUNDELL, dissenting: I disagree on the last point—the treatment of brokers' commissions. In my opinion the majority report errs in failing to allow the commissions to be deducted as ordinary and necessary expenses.

The facts stipulated abundantly establish that the taxpayer's activities in buying and selling securities amounted to a trade or business. Being engaged in a trade or business, it would seem that his expenses would be deductible under that section of the statute which allows the deduction of "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." Sec. 23 (a). It is difficult to see why commissions, particularly selling commissions, are not ordinary and necessary expenses. They are a part of the cost of selling goods, treated as such generally in business, and are allowed by the Commissioner's regulations to dealers in securities as distinguished from traders in that class of goods without expressed reason for the distinction. The statute makes no such distinction.

Earlier decisions are pointed to as establishing that commissions are not treated as expenses. Under the statutes in force when those decisions were rendered it mattered little what designation was given to them as long as they went into the computation of gain or loss. The practice of treating buying commissions as part of the cost and selling commissions as a reduction of selling price was in the interest of simplification of accounting for gains or losses and was without direct statutory sanction. Now that statutes have been enacted under which the taxpayer, following the former practice, can not
31 deduct as sustained loss, it seems to me that he should be permitted to call his expenditures by their true name—expenses of trade or business—and bring them within the statutory provision directly dealing with such expenditures. It is to be noted that section 23 (r), which is applied by the majority report to this case, does not deal with expenses at all, and, if there is any conflict between it and section 23 (a), then it should give way to the section directly dealing with expenses.

It is not a sound answer to the taxpayer's argument to say to him that possibly he may have the benefit of his expenses in a future year on other sales or exchanges. The taxing statutes have consistently assessed income taxes on the basis of annual accounting periods (Helvering v. Morgan's Inc., 293 U. S. 121) and in order to achieve this end it is necessary to account in each year for the profits or losses on the sale or exchange of all property dealt in within the

year. This requires that all profit on the property and all deductions allowed with respect to it be reported as occurring within the year. It is only when the deductions allowed for the year are exhausted that there is resort to the exception of carrying over to a succeeding year. Here, if we follow the plain wording of the statute and allow as expenses what are generally regarded as such, the taxpayer's operations within the year will be accounted for within that same year and thus meet the primary intent of Congress to levy taxes on an annual basis.

So far I have discussed mainly commissions of sales, for they are to my mind clearly business expenses. Commissions on purchases are a bit more difficult to classify, perhaps because we
32 have fallen into the habit of speaking of them as "capital expenditures." Yet upon analysis they are little if any different from selling expenses. To one engaged in the business of buying and selling they are ordinary and necessary expenses. A merchant employinig a buyer on salary would unquestionably deduct the salary as a current business expense rather than allocate it as part of the cost of goods, and in substance a commission paid to a buyer is no different.

LEECH, ARNOLD, and HARRON agree with this dissent.

BLACK agrees with this dissent insofar as it relates to selling commissions.

Before United States Board of Tax Appeals

[Title omitted.]

Motion to vacate decision of the Board

Filed April 5, 1937

Now comes the Petitioner in the above entitled cause, by his attorney Thomas M. Wilkins, Union Trust Building, Washing-
33 ton, D. C., and moves that the Board vacate its decision herein promulgated on March 31, 1937, and reconsider the issues therein involved.

The reasons for this motion are:

"(a) That the decision (pages 6 and 7 of the advance sheets) is predicated in substance upon a repealed statutory provision, namely, Section 23 (r) (2) of the Revenue Act of 1932 (quoted in full on page 3 of the Board's decision). Specifically the Board's decision advances and relies upon a wholly fallacious premise, namely that the stock losses disallowed as a deduction by paragraph (1) of Section 23 (r) may be allowed as a 'carry over' in computing petitioner's income in 1933 the succeeding taxable year under the provisions of Section 23 (r) (2) of the Act. This provision, which could not have become effective in any case until January 1, 1933, was expressly repealed effective as of January 1, 1933, by Section 218 (b) of the National Industrial Recovery Act.

"(b) That the decision of the Circuit Court of Appeals in Davis v. United States, — Fed. (2d) — (January 4, 1937), relied upon by the Board in support of its view that Section 23 (r) is constitutional, is in conflict with decisions of the Supreme Court of the United States in the cases of Stewart Dry Goods Company v. Lewis, 294 U. S. 550, 558, and the United States Glue Company v. Town of Oak Creek, 247 U. S. 321, 328, which held that in order not to violate due process of law, graduated rates of taxation must be
34 adjusted with reasonable approximation to the net earnings of the taxpayers. Petitioner therefore urges that Section 23 (r) of the act is unconstitutional in that it has the effect of destroying the reasonable ground for discrimination resulting from graduated normal taxes and surtaxes.

"(c) That Constitutional questions if present in any case need not be pleaded nor even raised as the court or the Board may raise such questions of its own motion. Weems v. United States, 217 U. S. 349, 362.

"Respectfully submitted.

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Attorney for Petitioner,
Union Trust Building, Washington, D. C."

35 Before United States Board of Tax Appeals

[Title omitted.]

Motion for rehearing

Filed April 20, 1937

Now comes the Petitioner in the above entitled cause, by his attorney, Thomas M. Wilkins, Union Trust Building, Washington, D. C., and moves that the Board grant a rehearing in the above case and reconsider its opinion of March 31, 1937.

The reasons for this motion are set forth in the attached brief.

Respectfully submitted,

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Attorney for Petitioner,
Union Trust Building, Washington, D. C.

36 Before United States Board of Tax Appeals

[Title omitted.]

Brief in support of motion for rehearing and reconsideration of opinion

Filed April 20, 1937

1

Compensation paid brokers for services rendered in connection with the purchase and sale of stocks in the course of the ordinary and necessary operations of a taxpayer's trade or business are deductible under section 23 (a)

Section 23 (a) of the Revenue Act of 1932 provides that there shall be deducted in computing net income, the ordinary and necessary expenses of carrying on any trade or business "including a reasonable allowance for salaries, or other compensation for personal services actually rendered * * * ."

It is clear that the evidence in this case abundantly establishes that this taxpayer

37 "in dealing on the stock exchange to the extent he was during the taxable year, was carrying on a trade or business within the meaning of the statute." L. T. Alverson, 35 B. T. A. 482, 488.

The record also shows clearly that he expended during the said year "for personal services actually rendered" to him during the said year, "compensation" in the form of commissions in the amount of $18,888, which the Board has disallowed.

The Board of Tax Appeals in its majority opinion rendered in this case on March 31, 1937, refused to allow as deductions, the said "compensation" paid by Mr. Winmill during 1932 in carrying on his trade or business of buying and selling stocks. It cites the regulations having to do with the cost of capital assets purchased not in connection with a trade or business, and wholly ignores Article 121 of Regulation 77, which provides in part that "among the items included in business expenses are * * * commissions, * * *" etc.

In no case which has come to the attention of petitioner's counsel involving commissions on stocks purchased in the course of the operation of a trade or business have the regulations cited by the Board ever been applied by any court or by the Board of Tax Appeals.

Each of the cases cited by the Board in support of its majority opinion quite obviously relates to a strictly capital or casual matter and in no instance whatsoever to commissions paid on the purchase or sale of stocks bought and sold in the operation of a trade or business.

38 Specifically in the case of E. P. Greenwood, 34 B. T. A. 1209, the Board held expressly that Greenwood was not engaged in a trade or business; that the stock sales in issue were mere

casual sales and the Board disallowed the commissions in the year paid specifically on these grounds alone.

In the case of Florence G. Baldwin, 23 B. T. A. 512, the petitioner was not in the business of dealing in securities and therefore it was held that the commissions paid were not ordinary and necessary business expenses. The commissions were allowed by the Board in the year of the sale.

In the case of I. N. Burman, 23 B. T. A. 639, the commissions involved were commissions on casual purchases of real estate which was not sold during the taxable year. The Board in that case relied solely upon the decision in Hutton v. Commissioner, 39 Fed. (2d) 459.

In the case of Frank Cavanaugh, 19 B. T. A. 1251, the commissions involved were also real estate commissions on casual sale of real estate by a person who was not engaged in the purchase and sale of real estate as a business.

In the case of Hutton v. Commissioner, 39 Fed. (2d) 459, supra, the stocks casually purchased by Mrs. Hutton were not sold during the year, nor were they purchased as part of the operation of a trade or business carried on by her.

In the case of Helvering v. Union Pacific Railroad Company, 293 U. S. 282, the issue involved the deduction of commissions on bonds issued by the taxpayer itself. Each of the cases cited in the margin by the Supreme Court of the United States in support of its
39 tacit approval of the regulations providing for the capitalization of commissions, involved a commission paid on a clearly capital transaction such as a commission on the sale of capital stock being originally issued by the corporation taxpayer.

In its decision the Supreme Court pointed out, as did the Circuit Court of Appeals in the Hutton case, that the taxpayer suffered no hardship by such a rule and that the commission would eventually be reflected against income when the securities were eventually retired or sold. The same lack of hardship is obvious in every single case relied upon by the Board. In none of these cases could the provision of prior law corresponding to Section 23 (a) have been applicable.

Neither these cases nor the regulations have any application to the case of commissions expended by one carrying on the trade or business of buying and selling securities.

Even if we assume that the regulations and the decisions cited by the Board under laws prior to the 1932 act clearly prevented the deduction of commissions paid for services rendered in connection with the purchase and sale of securities in the course of the operation of a trade or business, these regulations and decisions are not applicable under the 1932 law, because of the fundamental change effected by Section 23 (r) (1).

It is true that legislative re-enactment of a statute without change operates as an implied legislative approval of the construction given to the statute before re-enactment, but where, as in the instant case,

the statute is re-enacted with a substantial change which eliminates the application of a uniformly expressed ground for the previous construction, such previous construction cannot apply to
40 the subsequent dissimilar enactment.

In DeGaney v. Lederer, 239 Fed. 568, 571, affirmed by the Supreme Court of the United States in 250 U. S. 376, the lower court said:

"Legislative constructions of prior acts have all the value of expressions of opinion by those to whose opinions weight and importance is attached. Inasmuch, however, as such an opinion is that of an autocrat who can impose his will by changing the law, the distinction must always be observed between an opinion of what the law has been and a new enactment. If such subsequent statute gives to the prior one a meaning different from its sound meaning as judicially construed, the later statute is a new enactment, no matter what its form."

See "Statutes" 59 Corpus Juris 1063 and 1064 indicating clearly that where the old and new statutes are essentially dissimilar the rule that the construction placed on a former statute by the courts is impliedly adopted by the legislature when it re-enacts such statute or enacts analagous legislation, does not apply.

Inasmuch as the regulations and decisions relied upon by the Board in support of its majority opinion all clearly contemplate the eventual allowance against income of the commissions paid in connection with capital purchases and sales, and as the higher court decisions cited predicate their holding on the premise of eventual allowance against income, the said regulations and decisions
41 are not authority to completely and forever disallow this compensation paid in the operation of a trade or business contrary to the plain language of section 23 (a).

In this regard the quotation by the majority opinion of the Board from the decision of the U. S. Supreme Court in the case of DeGaney v. Lederer (supra), is quite appropriate:

"Unless the contrary appears, statutory words are presumed to be used in their ordinary and usual sense, and with the meaning commonly attributable to them."

The words "compensation for personal services" as used in section 23 (a) of the Revenue Act of 1932 are presumed to be used in their ordinary and usual sense and with the meaning commonly attributable to them. In that sense and with that commonly attributable meaning, these words include compensation in the form of broker's commissions and when such compensation is paid in connection with the purchase and sale of stocks bought and sold in the course of the ordinary and necessary operations of a taxpayers' trade or business, the statute requires that said compensation for services actually rendered shall be allowed as a deduction in computing income.

Prior to the opinion of the Board in the Winmill case there was no authority to the contrary by the Board or any court.

The Board in its majority opinion contends that the cases cited by it are applicable to the case of this taxpayer because he "suffers no

hardship by the ruling adopted by it as to commissions." The
42 Board relies upon the carry over provisions of section 23 (r) (2) of the Revenue Act of 1932 as authority for that view. However, this argument which is indispensible to the application of the decisions cited and to the Board's majority opinion is completely refuted by the fact that the carry over provisions of Section 23 (r) (2) of the act never went into effect because they were repealed by the National Industrial Recovery Act as of January 1, 1933—the first day on which these provisions ever could have been made effective. It is therefore definitely not a fact, as stated by the Board, that he "suffered no hardship by the ruling adopted by it as to commissions."

II

Section 23 (r) (1) is invalid because, if upheld, results in a tax at progressive rates on gross income. Stewart Dry Goods Co. v. Lewis, 294 U. S. 550

With respect to the argument that the provisions of Section 23 (r) are unconstitutional in that they violate the due process clause of the Fifth Amendment to the Constitution, it is believed that the Board did not have brought to its attention the decisions of the Supreme Court of the United States in Stewart Dry Goods Co. v. Lewis, 294 U. S. 550 and United States Glue Co. v. Town of Oak Creek, 247 U. S. 321, which decisions are clearly inconsistent with the decision of the Circuit Court of Appeals in Davis v. U. S., 87 Fed. (2d), 323, relied upon in support of the majority opinion of the Board.

43 The provisions of Section 23 (r) (1) have the effect of applying the progressive rates of income tax without relation to the taxpayer's ability to pay. This circumstance destroys the reasonable basis for the discrimination otherwise inherent in the progressive income tax rate schedule. The only constitutional justification for the application of a graduated scale of rates in income taxation is the superior ability to pay of those upon whom the higher rates are imposed. Graduated rates must bear a reasonable relation to the current increase in net worth of the taxpayer resulting from transactions completed during the taxable year.

Losses of a taxpayer which occur in his trade or business reduce his net worth. They are definitely related to his taxable profits from other activities for the same year (a) as to the purpose to make a profit, (b) as to the taxable year involved and (c) as to the taxable person. Such losses must, therefore, be taken into account in applying a schedule of graduated rates based on ability to pay. Mr. Winmill had an actual loss of $135,000 during the taxable year, yet under the statute he must pay a tax on that loss as though he had a net income of $35,000.

The general principles governing this phase of the case were clearly stated by the Supreme Court in the case of Stewart Dry Goods Co. v. Lewis, 294 U. S. 550, 558, in which the Court said:

"The district court found that 'generally speaking' he who sells more is in receipt of a greater profit and hence has larger abil-
44 ity to pay, and upon this basis justified the classification. But it is to be remembered that the act in question taxes gross sales and not net income. As stated in United States Glue Co. v. Town of Oak Creek, 247 U. S. 321, 328:

" 'The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large.'

* * * * * * *

"The proofs submitted are insufficient to support the appellees' contention that the graduation of the tax was adjusted with reasonable approximation to the net earnings of the taxpayers.

* * * * * * *

"An income levy by its very nature assures equality of treatment, because the burden of the exaction varies with increase or
45 decrease of return on capital invested and with the comparative success or failure of the enterprise.

* * * * * * *

"As we have said, the statute does not purport to levy a tax on incomes. Plainly it does not in fact do so. A merchant having a gross business of $1,000,000, but a net loss, must pay a greater tax than one who has a gross of $400,000 and realizes a substantial net profit.

* * * * * * *

"The law arbitrarily classifies these vendors for the imposition of a varying rate of taxation, solely by reference to the volume of their transactions, disregarding the absence of any reasonable relation between the chosen criterion of classification and the privilege, the enjoyment of which is said to be the subject taxed. It exacts from two persons different amounts for the privilege of doing exactly similar acts because the one has performed the act oftener than the other.

"We hold the act unconstitutional."

It is therefore respectfully submitted that Section 23 (r) is unconstitutional because it results in a graduated tax on gross income

and thus discriminates between persons wholly without substantial reason based upon differences which bear no reasonable and just relation to the matter in respect of which the classification is proposed.

46 It is respectfully prayed that the Board reconsider its opinion of March 31, 1937, and determine that there is no deficiency against this taxpayer for the year 1932.

THOMAS M. WILKINS,
Attorney for Petitioner,
Union Trust Building, Washington, D. C.

Before United States Board of Tax Appeals.

Docket No. 79,036

ROBERT C. WINMILL, PETITIONER
v.
COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to findings of fact and opinion herein promulgated March 31, 1937, directing that the deficiency be determined and decision entered under Rule 50, respondent on April 28, 1937, filed a proposed determination of deficiency and notice thereof, which were duly served upon petitioner; and petitioner having filed, on April 30, 1937, notice of acquiescence to said proposed determination, it is

Ordered and decided that there is a deficiency in income tax herein for the year 1932 in the amount of $5,508.14.

(Signed) ARTHUR J. MELLOTT, *Member.*

Enter:
Entered May 3, 1937.

47 In United States Circuit Court of Appeals for the Second Circuit

[Title omitted.]

Petition for review

Filed July 6, 1937

To the Honorable Judges of the United States Circuit Court of Appeals for the Second Circuit:

Now comes Robert C. Winmill by his Attorney, Thomas M. Wilkins, Union Trust Building, Washington, D. C., and in support of this his petition filed in pursuance of the provisions of section 1001 of the Revenue Act of 1926 as amended, for the review of the decision of the United States Board of Tax Appeals rendered on May 3, 1937, redetermining as to this petitioner, Robert C. Winmill, that there is

a deficiency in income tax for the year 1932 in the amount of $5,508.14, respectfully shows to this Honorable Court as follows:

I. DESIGNATION OF COURT OF REVIEW

The petitioner on review is an individual with his place of
48 business at One Wall Street, New York, New York. On or about March 15, 1933, this petitioner filed a Federal income tax return for the calendar year 1932 with the Collector of Internal Revenue for the Second District of New York, with offices located in New York City, and within the judicial circuit of the United States Circuit Court of Appeals for the Second Circuit.

The petitioner being aggrieved by the findings of fact, opinion, decision and order of the United States Board of Tax Appeals in the above-entitled case, and the Collector's Office, to which was made the return of the income tax in respect of which the liability in controversy arises, being located within the Second Judicial Circuit; the petitioner desires a review of said findings of fact, opinion, decision and order, in accordance with the provisions of the Revenue Act of 1926, as amended, by the United States Circuit Court of Appeals for the Second Circuit.

II. PRIOR PROCEEDINGS

The Commissioner of Internal Revenue determined a deficiency in income tax against said petitioner in the amount of $5,508.14 for the calendar year 1932, and on January 14, 1935, sent to the said petitioner by registered mail, a notice of the said determination of income tax deficiency as provided in Title III of the Revenue Act of 1926 as amended. Subsequently, on April 10, 1935, the petitioner filed with the United States Board of Tax Appeals a petition appealing from the said determining contesting the entire amount of the said deficiency determined by the Commissioner as aforesaid. On
49 April 27, 1935, the Commissioner filed an answer to the petition admitting the jurisdictional facts set forth in the petition, but entering a general denial as to facts set forth in support of the petitioner's contention that there was no deficiency in income tax for the said calendar year 1932.

On September 9, 1935, the Board served notice upon the parties that the proceeding had been set down for hearing before the Board in Washington on October 28, 1935.

On October 16, 1935, the petitioner filed a motion with the Board requesting that the case be set down for hearing in the vicinity of New York City. Under date of October 18, 1935, the said motion was granted by the Chairman of the Board and the case was set down for hearing in New York City and was heard by the Board on May 12, 1936.

On March 31, 1937, the Board promulgated its opinion and on May 3, 1937, entered its final decision wherein it was ordered and decided

that there was a deficiency in Federal income tax against said petitioner for the calendar year 1932 in the amount of $5,508.14.

III. NATURE OF THE CONTROVERSY

Petitioner, a member of a partnership engaged in the stock brokerage business, operated three securities trading accounts as an individual and also operated four accounts jointly with others. During the taxable year he reported a gain from his partnership interest and from the operation of the joint accounts and a large loss from the operation of his individual accounts. All of the securities sold
50 were non-capital assets. In computing the amount of the loss and gain on these accounts, buying commissions were included as part of the cost and selling commissions as an off-set against the selling price.

The petitioner contended before the Board.

(a) That there should be no deficiency, because section 23 (r) of the Revenue Act of 1932, under which the Commissioner disallowed the stock losses claimed as a deduction on petitioner's return, is unconstitutional and void, under Article I, section 2, clause 3 and section 9, clause 4, (1) because it levies a direct, unapportioned tax upon subject matter not contemplated by the word "incomes" within the meaning of the Sixteenth Amendment to the Constitution, (2) because said section 23 (r) of the Revenue Act of 1932 is unconstitutional and void under the due process clause of the Fifth Amendment in that it causes the tax imposed by the Act to unreasonably discriminate between taxpayers selling stocks and bonds and taxpayers selling other property held less than two years, and (3) that the said section 23 (r) is unconstitutional and invalid under the Fifth Amendment, because if upheld it results in imposing a tax on gross income at progressive rates of surtax, without reference to the ability to pay.

(b) That even if the statute is constitutional, the brokers' commissions in the total amount of $19,028.75, which the petitioner was required to pay in connection with the purchase and sale of the 61,992 shares of stock sold by him during the year 1932, represented
51 ordinary and necessary expenses paid by the petitioner in the course of the trade or business carried on by him in pursuance of which the said 61,992 shares of stock were purchased and sold by him during the year 1932.

(c) That there is no authority under the law for increasing the petitioner's income for the year 1932 by an amount equal to the stock profits on joint accounts of $2,247.65 by refusing to allow as a deduction an equal amount of losses from sales of stocks and bonds by petitioner.

IV. ASSIGNMENT OF ERRORS

Your petitioner says that in the record and proceedings of the United States Board of Tax Appeals in the above-entitled cause and in the final order entered therein there is manifest error, and for error the petitioner assigns the following:

(1) The Board erred in holding that there is a deficiency for the calendar year 1932 in the amount of $5,508.14 or any other amount.

(2) The Board erred in holding the provisions of the Revenue Act of 1932 and particularly 23 (r) thereof, to be constitutional.

(3) The Board erred in refusing to allow as a deduction buying and selling commissions paid by the petitioner during the calendar year 1932, in the total amount of $19,028.75 in buying and selling shares of stock during the said year 1932 in carrying on his trade or business of operating three separate security trading accounts,
52 the entire interest in each of which was his own, and his four joint accounts in which others had a half interest.

(4) The Board erred in disallowing brokers purchase or buying commissions paid on the purchase of the said 61,992 shares of stock sold during the year 1932 in the amount of $9,181.00.

(5) The Board erred in disallowing brokers selling commissions in the amount of $9,574.00, paid during 1932 on the sale of the said 61,992 shares of stock sold during the year 1932.

(6) The Board erred in not holding that the operation by petitioner during 1932 of the said three separate security trading accounts, the entire interest in each of which belonged to the petitioner, was a "trade or business" within the meaning of those words as used in section 23 (a) of the Revenue Act of 1932.

(7) The Board erred in not holding that the operation by petitioner during 1932 of each of his four joint security trading accounts, a half interest in each of which belonged to others, was a "trade or business" within the meaning of those words as used in section 23 (a) of the Revenue Act of 1932.

(8) The Board erred in not allowing as a deduction under section 23(e) of the Revenue Act of 1932, losses in the amount of $155,989.92 from sales of stocks and bonds held by petitioner for less than two years in the three separate trading accounts, the entire interest in each of which was his own.

53 (9) The Board erred in not allowing as a deduction under section 23 (e) of the Revenue Act of 1932, losses from sales of stocks and bonds held for less than two years in the three separate trading accounts operated by the petitioner during 1932, the entire interest in each of which was his own, to the extent of $2,247.65, or an amount equal to the petitioner's stock profits in his joint accounts.

(10) The Board erred in increasing petitioner's income by $2,247.65 on the basis of its holding in effect that regardless of the provisions of section 23 (r) of the Revenue Act of 1932, losses from sales of stocks and bonds held by petitioner for less than two years individually may not be allowed to the extent of the petitioner's share

in the gain from sales of stocks and bonds held jointly for less than two years.

PRAYER

Your petitioner therefore prays for review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the United States Board of Tax Appeals in the above-entitled case, in accordance with the act of Congress in such cases made and provided, and that the Clerk of the said Board be directed to transmit and deliver to the Clerk of the said Court certified copies of all and every of the documents listed and set forth in the rules adopted by the United States Circuit Court of Appeals for the Second Circuit providing for the presentation of petitions for review of decisions of the United States Board of Tax Appeals.

54 And your petitioner will ever pray.

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Counsel for Petitioner,
Union Trust Building, Washington, D. C.

[*Duly sworn to by Thomas M. Wilkins; jurat omitted in printing.*]

55 In United States Circuit Court of Appeals, for the Second Circuit

Proof of service

Filed July 6, 1937

[Title omitted.]

To MORRISON SHAFROTH,
Chief Counsel, Bureau of Internal Revenue:

Please take notice that the petitioner on review on the 6th day of July 1937, filed with the Clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled cause. A copy of the petition for review and the assignment of errors as filed is hereto attached and served upon you. Dated at Washington, D. C., this 6th day of July 1937.

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Counsel for Petitioner on Review,
Union Trust Building, Washington, D. C.

56 Personal service of the above and foregoing notice, together with a copy of the petition for review and assignment of errors mentioned therein, as acknowledged this 6th day of July 1937.

(Signed) Morrison Shafroth,
MORRISON SHAFROTH,
Chief Counsel,
Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket No. 79,036

ROBERT C. WINMILL, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Statement of evidence

Filed July 15, 1937

This cause came on to be heard before the United States Board of Tax Appeals on May 12, 1936, at New York, New York, the Honorable Arthur J. Mellott, Member of the United States Board of Tax Appeals presiding. Thomas M. Wilkins, Esq., appeared on behalf of petitioner and John H. Pigg, Esq., appeared on behalf of the Commissioner. The following is a narrative statement of the evidence to the Board.

57 The petitioner conceded in open court that the income of the Gude, Winmill partnership was derived solely and exclusively from commissions from the sale of stock or interest or both.

ROBERT C. WINMILL, called as a witness by and on behalf of the petitioner, having been first duly sworn, testified on direct examination as follows:

My business is that of stock broker in the firm of Gude, Winmill and Company. During 1932 I was a partner in that firm and I traded considerably for my own account, bought and sold securities. During 1932 I traded to a considerable extent for my own account. I spent a considerable amount of my time on the trading. To elaborate on the answer, I had seven partners, the business was very dull then, and I traded a great deal for myself. In trading during that year, I had some joint accounts with others. As to the nature of those joint accounts, there were no contracts. We had some trades with others, jointly with them, and we shared the profits and losses together. They didn't amount to a great deal, but the figures show there, I ran them, and handled the business of the accounts. I gave the orders in both cases. As to the discretion used in giving those orders, it was my discretion, I don't know whether in every case it was entirely my discretion, it was four years ago. I do not remember whether or not I was influenced at all by the person with
58 whom I was engaged in this joint venture in every case, it was four years ago. In my own personal account I was not influenced by anyone.

Cross examination of Mr. WINMILL:

As a member of the partnership of Gude, Winmill and Company during the year 1932 I was at the office and I devoted a great deal of my time to my own business, because, you see, a great deal of my own time was spent in the partnership business, but not as much as I spent in my own business. My partnership was a stock brokerage firm which bought and sold for customers only, purely a commission

house for customers for a commission. To some extent, as a member of the partnership or as an officer of the organization, I saw customers and made and handled transactions for them as a member of the partnership. This was done to some extent during 1932, as you know, was a very bad year, our income was very low and business was very, very bad. It would be very hard to state approximately how much of my time was spent during 1932 as a member of the partnership receiving orders and taking orders for the purchase and sale of stock for customers. There weren't so many orders, that is the unfortunate part of it, business was very, very slow, we ran in the red to a great extent during the year. I spent a great deal of my time, I regret to say, in my own trading. It didn't prove very profitable. The records would show much better than I can tell whether the 419 sales of stock effected by me during 1932, occurred in a short
59 period of time or whether they were more or less continuous throughout the year, I couldn't positively say. I devoted a great deal of my time to these individual stock transactions, but I can't say definitely how much time I devoted to them. I was absent from New York City at sometime during the year 1932, as to how long I would have to look that up. I generally go away every year for a while, I don't recall 1932. I did go abroad during the year 1932. I don't remember just exactly how long I was absent from the United States during that year. I know we rented our place down on Long Island, and I was away part of that summer. I frequently spend a little of my time in Warrenton, Virginia. I don't know about how much each year. We have an office down there, a branch office, and when I am down there I go to the office. I imagine every day I am down there, I do that, but we have had a branch down there for ten years or more. I mean a branch office of the partnership of Gude, Winmill and Company in Warrenton. So I can go in there and do any trading I have down there, or here. I handled through the branch office of the partnership, of which I am a member. All my business was done through Gude, Winmill and Company. I didn't maintain any individual office down there in which I carried on my own business with respect to these individual transactions. I had a desk down there, and a room in this building in which our office was located, of my own. I think it was a part of the partnership office, I imagine it was in the office, yes. I didn't pay the rent personally, I don't think so. I stated that I gave the order for the sale of the stock with these four joint trading
60 accounts described in the stipulation of facts. As to what consultation I had with the other persons associated with me or interested in those accounts, it might have come up in any way. We might have talked together and decided to do something. Whatever was done, I don't remember just the facts. One was with a fellow named Dick Height, that is dead now, and he used to come down to Warrenton once in a while and we used to see him once in a while and we had some joint accounts, we traded a little bit. I don't know just what the conversations were, they were speculations just the same as my own speculations in every way.

I was speculating with my money and my money was used in every joint account, I think, to carry the account, not the capital of the firm, but some individual money I had, the office was used for trading. As to whether or not the other persons with whom I was interested in these various accounts put their money into it to purchase certain shares of stock, I don't believe Dick Height, for instance (we had some accounts), I don't believe he ever spent any money, I don't believe he sent any money to the office; I margined the thing myself and ran the thing, and handled it and gave him half the profits. As to whether or not there was any agreement between us, and as to what the responsibility of the other person would be in the event of unfavorable outcome, he would take half the profit or the loss, just as the case might be. It was not very extensive, just little things, I mean we might start anything, they were very mild little trade, all of them, you can see they were nothing com-
61 pared with my own. I do not mean to testify that I gave him half the profits that arose from that account. He had a half interest in the account. He had a half responsibility and half the profit and half the losses, in every case, and they were all men of responsibility.

Redirect examination of Mr. WINMILL:

My office in Virginia was kept open all during the year. I don't think it has ever been closed since it was opened. It was opened about ten years ago, I think. In these transactions, these stock transactions, the joint transactions and my own individual transactions, the primary purpose of entering into them was to make money, profit.

The foregoing condensed statement of the evidence is hereby approved to be incorporated in the record on the petition for review, this 15th day of July, 1937.

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Union Trust Building, Washington, D. C.,
Attorney for the Petitioner.

(Signed) Morrison Shafroth,
MORRISON SHAFROTH,
Chief Counsel,
Bureau of Internal Revenue, Washington, D. C.,
Attorney for Respondent.

Approved and ordered filed this 15th day of July, 1937.

(Signed) Arthur J. Mellott,
ARTHUR J. MELLOTT,
Member, U. S. Board of Tax Appeals.

62 *Joint exhibit 1-A*

In re: Robert C. Winmill, Docket No. 79,036

The following schedule shows the result of the operations of the three stock trading accounts which were operated by the petitioner for his own account:

	Cost of stock sold in 1932 through three individual accounts	$2, 883, 773. 95
	Premiums paid on individual accounts, 1932	395. 51
	Premiums paid on individual accounts, 1932	361. 68
	Cost plus premiums on stock s. ld in 1932 on three individual accounts	$2, 884, 531. 14
	Selling price of 61,992 shares sold through three individual accounts	$2, 719, 760. 69
	Premiums received on sales through three accounts	1, 929. 67
	Premiums received on sales through three accounts	1, 214. 01
	Selling price, plus premiums received on sales through three accounts	$2, 722, 904. 37
	Cost as indicated above	$2, 884, 531. 14
	Selling price as indicated above	2, 722, 904, 37
	Loss on sales through three individual accounts, including tax but not including commissions	$ 161, 626. [illegible]
63	Buying commissions on stock sold in 1932, through three individual accounts	8, 911. 00
	Selling commissions on stock sold in 1932, through three individual accounts	9, 574. 00
	Loss on sales through three individual accounts, including tax and commissions	$180, 111. 77
	Tax paid in 1932 on 1932 sales through three individual accounts	5, 072. 95
	Loss on sales through three individual accounts, including commissions but not tax (taxes claimed and allowed as deductions)	$175, 038. 82
	Gain on sales through four joint stock trading accounts attributable to petitioner's interest	2, 267. 80
	Net loss claimed on 1932 return on account of three individual accounts and four joint-stock trading accounts	$172, 771. 02

The following schedule shows the petitioner's share of the result of the operations of the four joint stock trading accounts in which the petitioner had an interest, and which accounts were operated as joint ventures:

64	Cost of stock plus buying commissions		$68, 570. 00
	Buying commissions		270. 00
	Net cost of stock		$68, 300. 00
	Cost of calls		509. 50
	Cost of stock plus calls		$68, 809. 50
	Selling price less commissions and taxes		$71, 347. 30
	Selling commissions		273. 75
	Taxes on sales		66. 83
	Total selling price including commissions and taxes		$71, 687. 88
	Cost of stock plus calls as indicated above		68, 809. 50
	Gross profit on sales		$2, 878. 38
	Less: Taxes	$66. 83	
	Commissions	543. 75	
			610. 58
	Net gain on sales eac 5/12/36		$2, 267. 80

65

FILED

INDIVIDUAL INCOME TAX RETURN

For Calendar Year 1932

3148

891371

272

5,605.14

ROBERT C WINMILL

1 WALL ST

6-39 NEW YORK N.Y. N.Y.

Yes

INCOME

RECEIVED MAR 15 1933

DEDUCTIONS

COMPUTATION OF TAX

AFFIDAVIT

27

SCHEDULE A—[illegible] (See Instruction [illegible])

[illegible]

SCHEDULE B—[illegible]

[illegible]

SCHEDULE C—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction [illegible])

[illegible]	1930	[illegible]	[illegible]				[illegible]

SCHEDULE D—CAPITAL NET GAIN OR LOSS FROM SALE OF ASSETS HELD MORE THAN TWO YEARS (See Instruction [illegible])

[illegible]

SCHEDULE E—INTEREST ON LIBERTY BONDS AND OTHER OBLIGATIONS OR SECURITIES (See Instruction [illegible])

[illegible]

SCHEDULE F—EXPLANATION OF DEDUCTIONS CLAIMED IN ITEMS [illegible], 14, 16, 17, AND 18

Item 14 [illegible] Tax 5161.64 State Tax [illegible] [illegible] Tax 5427.15

Item 18 [illegible] 1-1930 [illegible] 25000.00
[illegible] 1932

EXPLANATION OF DEDUCTION FOR DEPRECIATION CLAIMED IN SCHEDULES A AND B

[illegible]

EXPLANATION OF DEDUCTION FOR LOSSES BY FIRE, STORM, ETC., CLAIMED IN SCHEDULE A, AND IN ITEM 15

[illegible]

67 Before United States Board of Tax Appeals

[Title omitted.]

Praecipe for transcript of record

Filed July 15, 1937

To the CLERK OF THE UNITED STATES BOARD OF TAX APPEALS:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Second Circuit, a certified transcript of the record on appeal and include therein, the following:

"(1) Docket entries of proceedings before the Board.

"(2) Pleadings before the Board as follows:

(a) Petition for redetermination filed April 10, 1935, including annexed copy of deficiency letter dated January 14, 1935.

"(b) Respondent's answer to amended petition filed April 27, 1935.

68 "(3) Opinion of the Board promulgated March 31, 1937, together with Mr. Arundal's descending opinion.

"(4) Motion to vacate decision of the Board filed April 5, 1937, and denied April 12, 1937.

"(5) Motion for re-hearing filed April 20, 1937, denied April 26, 1937.

"(6) Decision of the Board entered May 3, 1937.

"(7) Statement of evidence settled or agreed upon together with the following exhibits:

"'(a) Joint Exhibit A-1 showing in detail the result of the operations of seven trading accounts.

"'(b) Respondent's Exhibit A, individual income tax return for the calendar year 1932 of this petitioner.'

"(8) Petition for review filed July 6, 1937, together with proof of service of notice of filing petition for review, and service of copy of petition for review, dated July 6, 1937.

"(9) This praecipe."

The foregoing to be prepared, certified, and transmitted as required by law and the rules of the United States Circuit Court of Appeals for the Second Circuit.

(Signed) Thomas M. Wilkins,
THOMAS M. WILKINS,
Attorney for Robert C. Winmill.

JULY 15, 1937.

69 [Clerk's certificate to foregoing transcript omitted in printing.]

70 In United States Circuit Court of Appeals for the Second Circuit

No. 72—October Term, 1937

Argued Nov. 17, 1937. Decided Dec. 6, 1937

ROBERT C. WINMILL, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the Board of Tax Appeals

Before MANTON, L. HAND, and SWAN, Circuit Judges.

Petition to revise decision of the Board of Tax Appeals (35 B. T. A. 804). Decision reversed and remanded.

Thomas M. Wilkins, of Washington, D. C., for petitioner.

James W. Morris, Asst. Atty. Gen., and Sewall Key and Helen R. Carloss, Sp. Assts. to Atty. Gen., for respondent.

Opinion

MANTON, Circuit Judge.

Petitioner seeks a review of an income tax deficiency, charged against him for 1932. For several years prior to and during 1932, he was a member of a partnership engaged in the stock brokerage business. During 1932 petitioner ran three separate securities trading accounts which were his own. These operations involved 419 separate sales of 61,992 shares which had been acquired in 353 separate purchases. The cost of these shares was $2,884,531.14, exclusive of purchase commissions amounting to $8,911. Of this $8,911, $7,493.50 was paid in 1932 and $1,417.50 in 1931. On the sale of these shares, the return to him was $2,722,904.37, representing a loss. In 1932 he paid brokerage commissions of $9,574 on said sales. During 1932 petitioner also operated four other security trading accounts in each of which he had an interest. These were joint ventures with another person who shared in the profits or losses as they might occur. Petitioner, however, furnished all the capital needed in the operation of these four accounts. During the year there were sold, through these four accounts, 2,525 shares of stock in 22 separate sales transactions. These 2,525 shares had been acquired in 22 separate purchases. Petitioner's share in the cost of this stock was $68,300. The buying commissions paid by him in 1932 amounted to $270. Petitioner's share of the proceeds of stock sold through the four accounts was $71,687.88, and petitioner's share of the selling commissions paid during 1932 was $273.75. His share of the profits made in these four joint accounts during 1932 was $2,267.80 after payment of all costs and expenses. All shares sold through each of these seven accounts had been held less than two years, and hence were "non-

capital" assets under the 1932 Revenue Act (47 Stat. 192, § 101 (c) (8), 26 U. S. C. A. § 101 note). In his 1932 return, petitioner claimed the right to offset his share of the profits arising from the operation of the four accounts against the losses resulting from the three accounts and show a loss deductible from ordinary income. The Commissioner disallowed the deductions claimed on the petitioner's return and increased his income for the year 1932 by $2,267.80, the sum of the stock profit on the joint accounts, plus $172,771.02, which represented the stock losses in the three accounts. This resulted in the additional tax. No part of the broker's commissions referred to have been allowed by the Commissioner, as deduc-
71 tion. The petitioner kept his books and made his return for the year 1932 on a cash receipt and disbursement basis.

It is contended on this petition to review that section 23 (r) (1) of the Revenue Act of 1932, 26 U. S. C. A. § 23 note,[2] dealing with deductible losses from the sale of "non-capital" assets, permits him to include among his own "non-capital" gains his share of the joint venture's "non-capital" gains, where, as here, another party agreed with him, without furnishing any capital, to share equally with petitioner in the profits and losses resulting from such transactions as the joint venture might conduct. He also contends that, if section 23 (r) (1) of the Revenue Act of 1932 limits the deductibility of losses resulting from sales of stocks or bonds (which are "non-capital" assets) to gains from such sales during the taxable year, it is unconstitutional and void. Petitioner contends further that the buying and selling commissions paid were a necessary incident to the conduct of his business—trading in the market—and that, pursuant to section 23 (a) of the Revenue Act of 1932, 26 U. S. C. A. § 23 (a) and note,[3] he should be allowed these as deductions, even though such operations resulted in a loss and even though the losses from sales of "non-capital" assets are limited by section 23 (r) of the act, 26 U. S. C. A. § 23 note, to the gains from similar transactions.

The facts were stipulated, but the petitioner also testified that he devoted a portion of his time to the operation of these seven trading accounts.

Section 23 (r) places a limitation upon the deduction of losses. Congress has the power to condition, limit, or deny deductions from gross income in order to arrive at the net to be taxed. Burnet v. Thompson Oil & Gas Co., 283 U. S. 301, 51 S. Ct. 418, 75 L. Ed. 1049; Stanton v. Baltic Mining Co., 240 U. S. 103, 36 S. Ct. 278, 60 L. Ed. 546; Helvering v. Independent Life Ins. Co., 292 U. S. 371, 54 S. Ct. 758, 78 L. Ed. 1311. We held this provision of the statute constitutional in Davis v. United States (C. C. A.) 87 F. 2d 323. The petitioner may not offset his gains from the four joint accounts by his losses on the three accounts which he operated individually.

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[2] (r) Limitation on Stock Losses.
(1) Losses from sales or exchanges of stocks and bonds which are not capital assets shall be allowed only to the extent of the gains from such sales or exchanges.

[3] (a) Expenses.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered. * * *

Section 1111 (a) (3) of the Revenue Act of 1932, 26 U. S. C. A. § 1696 (2), defines "partnership" as including a "syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this Act [title] a trust or estate or a corporation; and the term 'partner' includes a member in such a syndicate, group," etc. Assuming that the petitioner and his associates in the joint ventures were not partners as generally accepted, they were nevertheless engaged in a "joint venture" in conducting these accounts and in dividing the profits and losses. For taxing purposes they must be considered as a "partnership." Johnston v. Com'r, 86 F. 2d 732 (C. C. A. 2). Accordingly, the Commissioner correctly ruled that the set-off could not be made.

Section 23 (a) of the 1932 Act (26 U. S. C. A. § 23 (a) and note) provides that there shall be deducted in computing net income, the ordinary necessary expenses of carrying on a trade or business "including * * * compensation for personal services actually rendered." The volume of sales and the amounts thereof and the time consumed in carrying on these operations would justify the Board of Tax Appeals in finding (they made no such finding) that the petitioner carried on these operations as a trade or business. During the year he expended "for personal services actually rendered to him" compensation in the form of commissions in the amount of $17,067.50 which the Board has disallowed. In such disallowance, the Board based its holding upon regulations having to do with "non-capital" assets not purchased in connection with a trade or business. Article 121 of the Treasury Regulations 77 provides in part that "among the items included in business expenses are * * * commissions. * * *" The allowance of commissions on real
72 estate sales as business expenses has been approved by the Board. The Highlands, Trust No. 1546 v. Com'r, 32 B. T. A. 760. See, also, Alexander Sprunt & Sons v. Com'r (C. C. A.) 64 F. 2d 424; Kornhauser v. U. S., 276 U. S. 145, 48 S. Ct. 219, 72 L. Ed. 505; Whitman v. Com'r, 16 B. T. A. 197, affirmed (C. C. A.) 49 F. 2d 1087 The same principle should be equally applicable to one whose trade and business involves the purchase and sale of stocks for profit.

Article 282 of Treasury Regulations 77 provides that commissions paid in purchasing securities are a part of the cost price of such securities while commissions paid in selling securities when such commissions are not an ordinary and necessary expense of carrying on a business are an offset against the selling price. If the petitioner's activities in buying and selling amounted to a trade or business, his expenses would be deductible under section 23 (a), 26 U. S. C. A. § 23 (a) and note, which allows "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." This would apply to commissions paid in buying and selling securities. No good reason is advanced for a discrimination against dealers in securities. The statute makes no such discrimination. The regulations and decisions which controlled the Board

in support of the majority opinion contemplate the eventual allowance against income of the commissions paid on purchases and sales not connected with a business.

The questions presented in Helvering v. Union Pacific Ry. Co., 293 U. S. 282, 55 S. Ct. 165, 79 L. Ed. 363, dealt with deductions of commissions on bonds issued by the taxpayer itself. The court then approved the regulation providing for the capitalization of the commissions involved. The taxpayer suffered no hardship by such a rule, as was pointed out in Hutton v. Com's, 39 F. 2d 459 (C. C. A. 5), since, under the Revenue Acts then in force, the commissions would be reflected against income when the securities were eventually sold. But under the 1932 Revenue Act, due to section 23 (r), 26 U. S. C. A. § 23 note, the commissions paid would not be reflected against gross income unless the sale of the securities resulted in a profit.

Section 23 (r), 26 U. S. C. A. § 23 note, does not deal with expenses at all, and there is no conflict between it and section 23 (a), 26 U. S. C. A. § 23 (a) and note. Nor may it be said that there is a possibility that the petitioner would have the benefit of his expenses in a future year on other sales or exchanges. Taxing statutes consistently assess income taxes on the basis of annual accounting periods. If the commissions be regarded as an expense of a trade or business, the petitioner's operations within the year will be accounted for within that same year, and this meets the intent of Congress to levy taxes on an annual basis. If a merchant employed a buyer, his salary would be deductible as a current expense and would not be allocated as part of the cost of the goods. If the merchant paid a commission instead of a salary, it would likewise be a necessary expenditure of the business. So, too, the commissions paid in the purchase and sale of securities are an expenditure of carrying on that business.

The decision is reversed and the cause remanded for the Board to make a finding as to whether or not the petitioner, in 1932, was a trader in the business of buying and selling securities. If so, the commissions for purchases and sales are deductible.

73 In United States Circuit Court of Appeals, Second Circuit

ROBERT C. WINMILL, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Judgment

Filed December 13, 1937

Appeal from the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the ——— order of said United States Board of Tax Appeals be and it hereby is reversed and cause remanded for further proceedings in accordance with the opinion of this court.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

WM. PARKIN, *Clerk*.

74 [File endorsement omitted.]

75 [Clerk's certificate to foregoing transcript omitted in printing.]

76 Supreme Court of the United States

Order allowing certiorari

Filed April 11, 1938

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

File No. 42,341. U. S. Circuit Court of Appeals, Second Circuit. Term No. 860. Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Robert C. Winmill. Petition for a writ of certiorari and exhibit thereto. Filed March 12, 1938. Term No. 860 O. T. 1937.

U. S. GOVERNMENT PRINTING OFFICE: 1938

No. [redacted] 11

In the Supreme Court of the United States

October Term, 1937

Guy T. Helvering, Commissioner of Internal Revenue, petitioner

v.

Robert C. Winmill

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX

CITATIONS

50575—38

In the Supreme Court of the United States

OCTOBER TERM, 1937

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ROBERT C. WINMILL

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above-entitled cause on December 13, 1937, reversing in part a decision of the Board of Tax Appeals.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 17-32) is reported in 35 B. T. A. 804. The opinion of the Circuit Court of Appeals is reported in 93 F. (2d) 494.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered December 13, 1937. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a taxpayer who is engaged in the business of buying and selling securities for his own account may deduct, as an ordinary and necessary business expense, brokerage commissions paid in the purchase of the securities, or whether such commissions represent a part of the cost of the securities.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> (a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *
>
> * * * * *

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

> ART. 282. *Capital expenditures.*—Amounts paid for increasing the capital value or for making good the depreciation (for which a deduction has been made) of property are

> not deductible from gross income. (See section 23 (k) and article 201.) Amounts expended for securing a copyright and plates, which remain the property of the person making the payments, are investments of capital. The cost of defending or perfecting title to property constitutes a part of the cost of the property and is not a deductible expense. The amount expended for architects' services is part of the cost of the building. Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in selling securities, when such commissions are not an ordinary and necessary business expense, are an offset against the selling price. * * *

STATEMENT

During the year 1932, the respondent operated three separate securities trading accounts (R. 19). During that year he paid, as brokerage commissions in the purchase of securities, the sum of $7,493.50 (R. 20). He also operated jointly with other persons four securities trading accounts. His share of the buying commissions paid by these joint ventures in 1932 was $270 (R. 20). He contends that these amounts are deductible as an ordinary and necessary business expense. The Commissioner of Internal Revenue determined that such commissions represented a part of the cost of the securities, and his action was affirmed by the Board of Tax Appeals (R. 29). Upon appeal, the Circuit Court of Appeals reversed and

remanded the cause with instructions to allow the commissions as an ordinary and necessary business expense, in the event the Board should find that the taxpayer was engaged in the business of buying and selling securities (R. 72).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that a taxpayer engaged in the business of buying and selling securities for his own account is entitled to deduct from gross income, as an ordinary and necessary business expense, brokerage commissions paid in the purchase of securities.

2. In failing to hold that brokerage commissions paid in the purchase of securities represent a part of the cost of such securities.

3. In reversing in part the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision of the Circuit Court of Appeals holding that a taxpayer engaged in the business of buying and selling securities for his own account is entitled to deduct, as an ordinary and necessary business expense, the brokerage commissions paid in the purchase of securities is in direct conflict with the decision of the Circuit Court of Appeals for the Fifth Circuit in *Hutton* v. *Commissioner*, 39 F. (2d) 459. In that case a taxpayer engaged in the business of "buying, holding, and selling realties, securities, etc.",

sought to deduct, as an ordinary and necessary business expense, brokerage commissions paid upon the purchase of certain securities. The court held, however, that such expenditures represented a part of the cost price of the securities and denied the deduction. In the instant case, under identical facts, the court held that the commissions were deductible.

2. The decision of the court below is inconsistent with decisions in analogous circumstances, such as its prior decision in *Bonwit Teller & Co.* v. *Commissioner,* 53 F. (2d) 381, certiorari denied, 284 U. S. 690, where it was held that commissions paid to secure a lease should be capitalized and deducted ratably over the life of the lease. The court in that case likened the commissions to a fee paid a broker for negotiating an annuity contract, and stated (p. 384) that such a fee "would pretty clearly be a capital expenditure to be added to the cost of the annuity rather than a business expense for the year when paid". To the same effect *Meyran* v. *Commissioner,* 63 F. (2d) 986 (C. C. A. 3d), and *Commissioner* v. *Chicago Dock & Canal Co.,* 84 F. (2d) 288 (C. C. A. 7th), holding that brokerage commissions paid for negotiating a lease are not to be treated as business expenses, even though, in the latter case, the business of the taxpayer was solely the making of leases.

3. The decision of the court below overturns the long established administrative practice of the Bureau of Internal Revenue with respect to the

handling of commissions paid upon the purchase of securities. The Treasury Regulations, beginning with those issued under the Revenue Act of 1916, have always provided that such commissions were not deductible as an expense, but were to be treated as part of the cost of the securities.[1] This long continued administrative construction may be deemed to have received legislative approval. *Brewster* v. *Gage*, 280 U. S. 327; *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459.

Moreover, the regulations were tacitly approved by this Court in *Helvering* v. *Union Pacific Co.*, 293 U. S. 282. In holding that commissions paid by a taxpayer for the sale of its own bonds were not deductible as ordinary and necessary expenses, this Court there said (p. 286):

> In this respect the commissions do not differ from brokerage commissions paid upon the purchase or sale of property. The regulations have consistently treated such commissions, not as items of current expense, but as additions to the cost of the property or deductions from the proceeds of sale, in arriving at net capital profit or loss for purposes of computing the tax.

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[1] See Par. 108, Treasury Regulations 33 (1916); Art. 293, Treasury Regulations 45 (1918); Art. 293, Treasury Regulations 62 (1921); Art. 292, Treasury Regulations 65 (1924); Art. 292, Treasury Regulations 69 (1926); Art. 282, Treasury Regulations 74 (1928); Art. 282, Treasury Regulations 77 (1932); Art. 24-2, Treasury Regulations 86 (1934); Art. 24-2, Treasury Regulations 94 (1936).

This Court cited the successive Regulations (293 U. S. at 286 note), including Article 282 of Regulations 77, which the court below declined to apply.

4. The enactment of Section 23 (r) of the Revenue Act of 1932, limiting deductions for non-capital losses to the amount of non-capital gains for the same year, does not militate against what has already been said. The court below pointed out that in view of Section 23 (r) a taxpayer might lose the benefit of any deduction for buying commissions with respect to securities if the commissions are required to be treated as items of cost reflected in gain or loss in the year of disposition rather than as a business expense in the year of acquisition. But even under prior revenue acts, in the absence of Section 23 (r), such treatment of buying commissions entailed a similar possibility, for if the securities were sold at a loss and no taxable income existed against which the loss might be taken in the year of sale, the commissions would serve no function in reducing taxable income, whereas they might have done so had they been treated as a business expense in the year of acquisition of the securities. The hazard is increased by virtue of Section 23 (r), but a hazard existed under the prior Acts. The regulations dealing with buying commissions have remained unchanged, and for the reasons indicated it is submitted that there was no necessity for change. The unwillingness of the court below to apply the provision of the reg-

ulations applicable in terms suggests, in any event, that the case is an appropriate one for review by this Court.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this petition should be granted.

ROBERT H. JACKSON,
Solicitor General.

MARCH, 1938

U. S. GOVERNMENT PRINTING OFFICE: 1938

No. 11

In the Supreme Court of the United States

October Term, 1938

Guy T. Helvering, Commissioner of Internal Revenue, petitioner

v.

Robert C. Winmill

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

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CITATIONS

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion and dissenting opinion in the Board of Tax Appeals (R. 8–16) are reported in 35 B. T. A. 804. The opinion of the Circuit Court of Appeals (R. 35–38) is reported in 93 F. (2d) 494.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered December 13, 1937 (R. 38–39). The petition for a writ of certiorari was filed March 12, 1938, and was granted April 11, 1938 (R. 39).

The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a taxpayer who is engaged in the business of buying and selling securities for his own account may deduct, as an ordinary and necessary business expense, brokerage commissions paid in the purchase of the securities, or whether such commissions represent a part of the cost of the securities.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions:
>
> (a) EXPENSES.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *
>
> * * * * *
>
> (r) LIMITATION ON STOCK LOSSES.—
>
> (1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) COMPUTATION OF GAIN OR LOSS.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) BASIS (UNADJUSTED) OF PROPERTY.—The basis of property shall be the cost of such property; * * *

* * * * *

(b) ADJUSTED BASIS.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) GENERAL RULE.—Proper adjustment in respect of the property shall in all cases be made—

(A) for expenditures, receipts, losses, or other items, properly chargeable to capital account, including taxes and other carrying charges on unimproved and unproductive real property, but no such adjustment shall be made for taxes or other carrying charges for which deductions have been taken by the

taxpayer in determining net income for the taxable year or prior taxable years;

* * * * *

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

ART. 103. *Inventories at cost.*—Cost means:

* * * * *

(2) In the case of merchandise purchased since the beginning of the taxable year, the invoice price less trade or other discounts, except strictly cash discounts approximating a fair interest rate, which may be deducted or not at the option of the taxpayer, provided a consistent course is followed. To this net invoice price should be added transportation or other necessary charges incurred in acquiring possession of the goods.

* * * * *

ART. 121. *Business expenses.*—Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except the classes of items which are deductible under the provisions of articles 141–272. The cost of goods purchased for resale, with proper adjustment for opening and closing inventories, is deducted from gross sales in computing gross income. (See article 55.) Among the items included in business expenses are management expenses, commissions, labor, supplies, incidental repairs, operating expenses of automobiles used in the

trade or business, traveling expenses while away from home solely in the pursuit of a trade or business (see article 122), advertising and other selling expenses, together with insurance premiums against fire, storm, theft, accident, or other similar losses in the case of a business, and rental for the use of business property. A taxpayer is entitled to deduct the necessary expenses paid in carrying on his business from his gross income from whatever source. As to items not deductible, see section 24 and articles 281–284.

ART. 282. *Capital expenditures.*—Amounts paid for increasing the capital value or for making good the depreciation (for which a deduction has been made) of property are not deductible from gross income. (See section 23 (k) and article 201.) Amounts expended for securing a copyright and plates, which remain the property of the person making the payments, are investments of capital. The cost of defending or perfecting title to property constitutes a part of the cost of the property and is not a deductible expense. The amount expended for architects' services is part of the cost of the building. *Commissions paid in purchasing securities are a part of the cost price of such securities.* Commissions paid in selling securities, when such commissions are not an ordinary and necessary business expense, are an offset against the selling price. * * * [Italics supplied.]

STATEMENT

During the year 1932 respondent operated three separate securities trading accounts (R. 9). During that year he sold 61,992 shares of stock through the three accounts, the cost of which to respondent was $2,884,531.14, exclusive of purchase commissions. The 61,992 shares were sold by respondent in 1932 for $2,722,904.37. Of the purchase commissions on the 61,992 shares, which amounted to $8,911, respondent paid $7,493.50 in 1932 (R. 9–10).

At the end of the year 1932 respondent had on hand in his individual trading accounts shares of stock on which purchase commissions in the amount of $403 were paid by him in that year. This amount is not included in the purchase commissions above described (R. 5, 10).

In his return for the year 1932 respondent claimed a deduction of $172,771.02 as losses on the sale of stocks (R. 9). In the audit of the return the Commissioner, relying on Section 23 (r) (1), *supra*, p. 2, disallowed the claimed deduction for stock losses and also refused to allow, as an alternative, the purchase commissions as a deductible expense (R. 6–7).

The Board of Tax Appeals sustained the Commissioner on both grounds (R. 8–15). It made no finding as to whether respondent was engaged in the business of buying and selling securities in 1932, since it believed that in any event the commissions were not deductible (R. 12–14). The Circuit Court of Appeals, holding that the commis-

sions were a business expense, ordered that the case be remanded to the Board for a finding on whether respondent was engaged in the business of buying and selling securities in 1932 (R. 38). Earlier in its opinion the court had stated that the evidence would justify such a finding (R. 37).[1] The petition for certiorari sought a review of the decision only so far as it related to the commissions paid on the purchase of shares of stock, in the amount of $7,896.50 ($7,493.50 plus $403).[2]

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that a taxpayer engaged in the business of buying and selling securities for his own account is entitled to deduct from gross income, as an ordinary and necessary business expense, brokerage commissions paid in the purchase of securities.

2. In failing to hold that brokerage commissions paid in the purchase of securities represent a part of the cost of such securities.

3. In reversing in part the decision of the Board of Tax Appeals.

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[1] The mandate of the Circuit Court of Appeals was not stayed. On December 31, 1937, the Board of Tax Appeals, pursuant to the remand, found as a fact that respondent was engaged in the business of buying and selling securities in 1932.

[2] The petition (p. 3) erroneously gives the total as $7,763.50 ($7,493.50 plus $270).

SUMMARY OF ARGUMENT

The Commissioner, in refusing to allow respondent to deduct brokerage commissions paid on the purchase of securities incident to a trade or business, followed the specific directions of Treasury Regulations 77, Article 282, which requires that such expenses be capitalized. The same requirement has appeared in every regulation since 1916, and must now be taken to have the force of law. Moreover, it has received judicial approval, and it is in accord with the principle that amounts paid in the acquisition of property are to be treated as a part of its cost.

The holding of the court below that Article 282 is limited by Section 23 (a) of the statute and Article 121 of the Regulations, promulgated under that section, is erroneous, for it is an obvious attempt to make a general regulation control a specific one. Moreover, general provisions similar to that of Section 23 (a) have been in the various Revenue Acts for many years, and hence the specific requirement of Article 282, which has been confirmed by Congress, must control.

The alternative holding below that Section 23 (r), which limits deductions for "non-capital" losses, deprives of force the reenactment of the statute in 1932, is also erroneous. That section changed only the consequences of the classification of expenditures as capital outlays or business expenses, not the classification itself, and was not, in

fact, a complete change even of consequences.

Moreover, even if Article 282 did not obtain a ratification by the reenactment of the statute in 1932, it is still in effect, and Section 23 (r) certainly does not so change the statute as to warrant a holding that the regulation is void. On the contrary, it seems plainly correct.

ARGUMENT

The sole issue in the present case is whether a taxpayer engaged in the business of buying and selling securities for his own account may deduct brokerage commissions paid in the purchase of securities as an ordinary and necessary business expense under Section 23 (a) of the Revenue Act of 1932, *supra*, p. 2, or whether they must be treated as a part of the cost of the securities. If they are treated as a capital expenditure, they simply increase respondent's loss on stock sales—a loss which he has not been allowed to deduct by reason of Section 23 (r) (1), *supra*, p. 2. If they be treated as a business expense, they may be deducted, since respondent had other income (R. 9).

The action of the Commissioner in treating these purchase commissions as capital expenditures, rather than business expenses, was based upon the clear mandate of Article 282, Treasury Regulations 77, *supra*, p. 5. That article provides in part as follows:

> Commissions paid in purchasing securities are a part of the cost price of such securities.

The regulation is clearly applicable and expressly denied the contention of the respondent.

Nor can its validity now be open to question. The regulations issued under the Revenue Act of 1916 stated that purchase commissions on securities were a part of the cost of the securities, and did not constitute expense deductions. See Art. 108, Treasury Regulations 33 (Revised, 1918). The same rule has been carried forward since that time, in substantially the same language, in every set of regulations dealing with income taxes that have been issued.[3] During that time the income tax has been constantly amended, deductions have been widely and frequently changed, and the very section of the statute under which this regulation was issued was amended three times prior to 1932, the year here involved.[4] It would be difficult to find a

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[3] Art. 293, Treasury Regulations 45 (1918); Art. 293, Treasury Regulations 62 (1921); Art. 292, Treasury Regulations 65 (1924); Art. 292, Treasury Regulations 69 (1926); Art. 282, Treasury Regulations 74 (1928); Art. 282, Treasury Regulations 77 (1932); Art. 24–2, Treasury Regulations 86 (1934); Art. 24–2, Treasury Regulations 94 (1936).

Since 1932, the regulations have been modified somewhat with regard to brokerage commissions paid on the sale of securities. That issue is not before this Court. In any event, that modification was applicable only to *dealers* in securities. See G. C. M. 15430, XIV–2 Cumulative Bulletin 59.

[4] Article 108, Regulations 33 (Revised, 1918) was issued under Section 5, Revenue Act of 1916 (c. 463, 39 Stat. 756). In the Revenue Act of 1918 (c. 18, 40 Stat. 1057), various items not deductible were gathered into Section 215. That section (which became Section 24 in the Revenue Act of 1928 and subsequent Acts) was itself twice amended: in the Revenue Act of 1921 (c. 136, 42 Stat. 227), by the addition

clearer case in which to apply the rule that Congress, by recension of the statute, must be presumed to have adopted its administrative interpretation, such that the regulation now has the force of law. *Old Mission Co.* v. *Helvering,* 293 U. S. 289, 294; *United States* v. *Dakota-Montana Oil Co.,* 288 U. S. 459, 466; *Hassett* v. *Welch,* 303 U. S. 303, 312.

Moreover, the regulation has received consistent judicial approval. In *Hutton* v. *Commissioner,* 39 F. (2d) 459 (C. C. A. 5th), the court, in approving and applying the regulation, pointed out (p. 460) that "It has been a settled rule of the Treasury Department that commissions paid in purchasing securities are a capital expenditure * * *." In *Helvering* v. *Union Pacific Co.,* 293 U. S. 282, this Court tacitly approved the regulation here in question. The Court held that commissions paid by a taxpayer upon its own bonds were not deductible as an expense in the year of issue, but should be amortized over the life of the bonds, and said (p. 286):

> In this respect the commissions do not differ from brokerage commissions paid upon the

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of Section 215 (b) and in the Revenue Act of 1928 (c. 852, 45 Stat. 791) by the addition of Section 24 (c).

Since 1932, the section has again been twice amended, with no indication that Congress was dissatisfied with the Commissioner's treatment of purchase commissions on securities. See Revenue Act of 1934 (c. 277, 48 Stat. 768), Sec. 24; Revenue Act of 1938 (Public No. 554, 75th Cong., 3d Sess.), Sec. 24.

> purchase or sale of property. The regulations have consistently treated such commissions, not as items of current expense, but as additions to the cost of the property or deductions from the proceeds of sale, in arriving at net capital profit or loss for purposes of computing the tax.

A footnotes to the opinion (Note 3, p. 486) cited the successive regulations, including Article 282 of Treasury Regulations 77, which the court below refused to apply.

Finally, the requirement that brokerage commissions paid in the purchase of securities be capitalized is in accord with the well-recognized principle that any amount paid in the acquisition or defense of title to property is a capital expenditure and is properly to be considered as a part of its cost. *Helvering* v. *Union Pacific Co., supra; Bonwit Teller & Co.* v. *Commissioner,* 53 F. (2d) 381 (C. C. A. 2d), certiorari denied, 284 U. S. 690; *Spinks Realty Co.* v. *Burnet,* 62 F. (2d) 860 (App. D. C.), certiorari denied, 290 U. S. 636; *Hutchings* v. *Burnet,* 58 F. (2d) 514 (App. D. C.); *Commissioner* v. *Chicago Dock & Canal Co.,* 84 F. (2d) 288 (C. C. A. 7th).[5] The regulations have, from the beginning, consistently so provided. See, *e. g.,*

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[5] Cf. *Beneficial Industrial Loan Corp.* v. *Handy,* 92 F. (2d) 74 (C. C. A. 3d), affirming 16 F. Supp. 110 (Del.); *Houston Natural Gas Corp.* v. *Commissioner,* 90 F. (2d) 814 (C. C. A. 4th), certiorari denied, 302 U. S. 722; *Baltimore & Ohio R. Co.* v. *Commissioner,* 78 F. (2d) 460, 463 (C. C. A. 4th); *Moynier* v. *Welch,* 97 F. (2d) 471 (C. C. A. 9th).

Article 103 (2), Treasury Regulations 77 (1932); Article 1613 (2), Treasury Regulations 69 (1926); Article 1582 (1), Treasury Regulations 45 (1918). See also Montgomery, *Auditing—Theory and Practice* (2d ed.), p. 383; Kester, *Accounting—Theory and Practice,* Vol. II, p. 282; I. T. 2433, VII-2 Cumulative Bulletin 130. In *Bonwit Teller & Co.* v. *Commissioner, supra,* it was held that commissions paid to secure a lease should be capitalized and deducted ratably over the life of the lease. The court likened the commissions to a fee paid a broker for negotiating an annuity contract and stated (53 F. (2d) at p. 384) that such a fee "would pretty clearly be a capital expenditure to be added to the cost of the annuity rather than a business expense for the year when paid." There appears to be no essential difference between a brokerage fee paid in the acquisition of an annuity contract and one paid in the acquisition of securities.

We submit, therefore, that Article 282 of the Regulations not only properly interprets the statute, but has also acquired, by the consistent reenactment of the section under which it was promulgated, a standing which may not now be questioned. Since it expressly comprehends the present case, the position of the Commissioner should be affirmed, and the decision below reversed.

The court below, in denying this contention, apparently sustained alternative arguments. First,

it held that Article 282 of the Regulations is modified by Section 23 (a) and Article 121, so that, properly interpreted, the regulations themselves sustain respondent rather than the Commissioner. Second, and in the event that Article 282 be considered applicable, the court held it to be erroneous, and not to be given weight as a consistent administrative construction of the statute because of the addition of Section 23 (r) to the statute in 1932. These arguments will be discussed in that order.

1. The argument that Article 282 is inapplicable to respondent rests upon the assumption that it is limited, in some fashion, by Section 23 (a) of the Act, *supra*, p. 2, and Article 121 of the Regulations, *infra*, p. 4, promulgated thereunder. Section 23 (a) allows the deduction of ordinary and necessary expenses involved in carrying on any trade or business. Article 121 provides, in part:

> Among the items included in business expenses are * * * commissions, * * *.

This, the court below held, authorized the deduction.

The difficulty with the argument is that it is obviously an effort to make a general regulation, which incidentally mentions "commissions," control a specific one, which requires that commissions paid in the purchase of securities be capitalized. That, of course, may not be done. Article 282 states, in language as clear as words can make it, that commissions paid in purchasing securities are a part of the cost of the securities. General language

elsewhere in the regulations can obviously not create an exception to that rule. Both the courts and the Board have denied that such an exception existed. *Hutton* v. *Commissioner, supra; I. N. Burman,* 23 B. T. A. 639, 643.

Moreover, to the extent that the decision below rests upon an interpretation of Article 121 which overrides Article 282, it is contrary to the Treasury's consistent interpretation of those provisions. And where the question is as to the proper construction of a Treasury regulation, the Treasury's own interpretation over a long period of years is the best evidence of what it intended the regulation to mean.

The argument based upon the general effect of Section 23 (a) might have some force but for the fact that some similar provision has existed in all the Revenue Acts. See, *e. g.,* Revenue Acts of 1921, 1924, Section 214 (a). Consequently, even on the assumption that Section 23 (a) could, in the absence of administrative construction, be construed to allow the deduction of purchase commissions paid in the course of a trade or business, the consistent reenactment of the statute without the express grant of a deduction expressly denied by the regulations must be taken as conclusive evidence that Section 23 (a) is not to be interpreted as a limitation on the provisions of Article 282. *Old Mission Co.* v. *Helvering; United States* v. *Dakota-Montana Oil Co.,* both *supra.*

2. Alternatively, the court below seems to have decided (R. 38) that whatever force may be attributed to prior reenactments of the Revenue Acts without modification of the rule of Article 282, the reenactment in 1932, the year applicable here, is of no effect because of the addition, in the Revenue Act of that year, of Section 23 (r), *supra*, p. 2. Of course, the fact that the reenactment of the statute did not constitute an approval of the regulation would not destroy its validity, and the article is still applicable to respondent whether or not it has been affirmatively approved. The court below, however, seems to have taken the further step, and held Article 282 to be a misinterpretation of the 1932 Act which need not be followed in the present case.

We believe the court erred in both respects. Section 23 (r) allows the deduction of losses from the sale or exchange of stocks which are not capital assets only to the extent of the gains from such sales or exchanges. When such gains are absent, as in the present case, purchase commissions which have been added to cost of securities will simply increase a loss which is not deductible. There is no reason to suppose, however, that Congress, simply by changing the *consequences* of a classification of expenditures as capital outlays, intended to modify the well-established classification itself. Indeed, the more reasonable inference is that it did not intend any modification, else it would have been at

pains to announce it. Cf. *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 466–467.

Actually Section 23 (r) did not work such a drastic change as respondent would have the Court believe. It is true that under that section a taxpayer might never have the benefit of a deduction of purchase commissions unless the sale of "non-capital" assets results in a profit, but even under prior Revenue Acts the requirement that purchase commissions be capitalized entailed a similar possibility. If securities were sold at a loss and no taxable income existed against which the loss might be taken in the year of sale, the commissions would serve no function in reducing taxable income, which they might have done had they been treated as a business expense in the year in which the securities were acquired. The hazard is increased by Section 23 (r), but a hazard existed under prior Acts. Bearing in mind the fact that deductions are a matter of legislative grace, *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435, 440, no great weight can be attached to the fact that the possibility of obtaining the benefit of a deduction has been decreased.

Moreover, even on the assumption that Section 23 (r) removes the effect of the reenactment of the statute, the court below seems completely unjustified in holding the regulation to be erroneous. As we have pointed out, *supra*, pp. 11–12, the regulation has received consistent judicial approval. *Helver-*

ing v. *Union Pacific Co.,* 293 U. S. 282, 286; *Hutton* v. *Commissioner,* 39 F. (2d) 459 (C. C. A. 5th). It is consistent with the administrative and judicial treatment of brokerage commissions paid upon the purchase of other property. See p. 12–13, *supra.* In fact, during the twenty years in which the Treasury Department has been requiring that purchase commissions on securities be capitalized, no court or Board decision has even intimated that the rule was erroneous. Under those circumstances, we submit, a regulation which *classifies* expenditures cannot be held void and of no effect simply because a change in the statute decreases the possibility of obtaining the benefit of a deduction if the classification remains in effect.

Finally, the conclusion that Section 23 (r) did not effect a change in the treatment of purchase commissions is reinforced by the unfairness that a contrary conclusion may bring to a much larger group of taxpayers than that in which respondent finds himself, namely, those who purchase securities in transactions not related to the prosecution of a trade or business. Hitherto, under the position asserted by the Government, such commissions have been added to cost and are revealed on the ultimate disposition of the securities. Now, however, the court below has classified purchase commissions as current expenses, rather than items of cost. If the decision below be affirmed, such commissions could not properly be added to cost; nor,

in the usual case, would they even be deductible as "expenses", because not incurred in a "trade or business". It is not to be presumed that Congress intended such far-reaching consequences to flow by implication from Section 23 (r).

CONCLUSION

The judgment of the Circuit Court of Appeals should be reversed.

Respectfully submitted.

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SEPTEMBER 1938.

U. S. GOVERNMENT PRINTING OFFICE: 1938

IN THE

Supreme Court of the United States

OCTOBER TERM, 1937.

No. [redacted] 11

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

ROBERT C. WINMILL, *Respondent.*

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF OF RESPONDENT IN OPPOSITION.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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CASES CITED.

Statute and Regulation:

IN THE

Supreme Court of the United States

OCTOBER TERM, 1937.

No. 860.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

ROBERT C. WINMILL, *Respondent*.

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF OF RESPONDENT IN OPPOSITION.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 17-32) is reported in 35 B. T. A. 804. The opinion of the United States Circuit Court for the Second Circuit is reported in 93 Fed. (2nd) 494.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered December 13, 1937. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

Whether a taxpayer who is engaged in the business of buying and selling securities for his own account may deduct buying commissions paid to brokers in the purchase of securities both bought and sold during the taxable year.

Statute and Regulation Involved.

Revenue Act of 1932, c. 209, 47 Stat. 169:

> Sec. 23. Deductions From Gross Income. In computing net income there shall be allowed as deductions:
>
> (a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

> Art. 121. *Business expenses.*—Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpxayer's trade or business, except the classes of items which are deductible under the provisions of articles 141-272. The cost of goods purchased for resale, with proper adjustment for opening and closing inventories, is deducted from gross sales in computing gross income. (See article 55.) Among the items included in business expenses are management expenses, commissions, * * *. etc.

Statement.

During the year 1932, the respondent operated three separate securities trading accounts (R. 19). During that year he paid, as brokerage commissions in the purchase of securi-

ties, which he sold during the year 1932, the sum of $7,493.50 (R. 19-20). He also operated jointly with other persons four securities trading accounts. His share of the buying commissions paid by these joint ventures in 1932 was $270. The securities on which these buying commissions were paid were sold during the year 1932 (R. 20). He contends that these amounts are deductible as an ordinary and necessary business expense. The Commissioner of Internal Revenue determined that such commissions represented a part of the cost of the securities, and his action was affirmed by the Board of Tax Appeals (R. 29). Upon appeal, the Circuit Court of Appeals reversed and remanded the cause with instructions to "make a finding as to whether or not the petitioner, in 1932, was a trader in the business of buying and selling securities. If so the commissions for purchases and sales are deductible." (R. 74)

Reasons for Denying the Writ.

The writ should be denied because there is no conflict between the decision of the court below under the 1932 Revenue Act and the decision of the Circuit Court of Appeals for the Fifth Circuit under the 1921 Revenue Act (42 Stat. 237) in *Hutton* v. *Commissioner*, 39 Fed. (2nd) 459. The commissions, as to which the petition for certiorari is directed, would be allowable clearly under the *Hutton* decision. Nor is there a conflict between the decision of the court below and any of the other decisions cited in the petition for certiorari. The decision is correct.

ARGUMENT.

I.

Under the *Hutton* decision the buying commissions in the amounts of $7,493.50 and $270 (as to which the petition for certiorari is directed) clearly would be allowable deductions because the securities on which these commissions were paid were sold during 1932. The court in the *Hutton* case spe-

cifically stated (p. 460) that the commissions paid in purchasing the securities may be deducted when the securities are eventually sold. Certainly certiorari on the ground of conflict with the *Hutton* case cannot be granted to review the deductibility of these commissions.

There is no conflict with *Bonwit Teller & Co.* v. *Commissioner*, 53 Fed. (2nd) 381, certiorari denied, 284 U. S. 690, *Meyran* v. *Commissioner*, 63 Fed. (2nd) 986 (C. C. A. 3rd) or *Commissioner* v. *Chicago Dock & Canal Co.*, 84 Fed. (2nd) 288 (C. C. A. 7th), because the property in each of those cases was a lease, the terms of which, in each case, ran for scores of years and it was anticipated that the benefits of the expenditures of the commissions would extend for many years after the taxable year. These expenditures were clearly in the nature of the capital expenditures intended to be provided for in Article 282 of Regulations 77 and are to be distinguished from the commissions specifically mentioned in Article 121 of Regulations 77, which are "ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business."

As correctly stated by the court below: "The questions presented in *Helvering* v. *Union Pacific Ry. Co.* (293 U. S. 282) dealt with deductions of commissions on bonds issued by the taxpayer itself. The court there approved the regulations providing for the capitalization of the commissions involved." (R. 74) Clearly therefore there is no conflict with that decision of this court. The commissioner's own regulations recognize that commissions are to be capitalized or expensed according to the purpose for which the property (on which the commission is paid) is acquired. If the property is being bought and sold in carrying on a trade or business, the commission is an expense. I. T. 2305, C. B. V-2, 108, The Highlands Trust, No. 1546, 32 B. T. A. 760. See also *Alexander Sprunt & Sons*, 64 Fed. (2nd) 424; *Kornhauser* v. *United States*, 276 U. S. 145, *Whitman* v. *Commissioner*, 16 B. T. A. 197, affd. 49 Fed. (2nd) 1087. If the property is being bought as a capital investment or to be

used over the years to produce income from such use, the commission is a capital expenditure and the authorities relied upon by the petitioner apply. No set rule can be prescribed based upon the *kind of property* on which the commission is paid. The circumstances and the purpose of acquisition in relation to its use must govern.

II.

While buying commissions on securities *not sold* during the taxable year would be deductible following the broad language of the opinion of the court below, under the 1932 Revenue Act, the disallowance under the 1921 Revenue Act, of such commissions, following the *Hutton* decision, does not constitute a conflict even in a general sense (as distinguished from a specific sense when applied to the particular commissions as to which the petition is addressed.)

Section 214 (a) of the Revenue Act of 1921 is in substance identical with Section 23 (a) of the Revenue Act of 1932 and contains the identical language quoted from the latter statute on page 2 hereof allowing "compensation for personal services" to be deducted. However, the court in the *Hutton* case ignored the plain language of the statute and disallowed the commissions of the taxpayer there, who was "engaged in the business of buying, holding and selling realties, securities, etc."

The reasons relied upon by the court in the *Hutton* case for ignoring the plain language of the act and for affirming what it considered to be the applicable rule of the Treasury Department (under which buying commissions were added to the cost of securities regardless of whether or not the commissions constituted business expenses) were: that the court had been referred to no decision contrary to the rule of the Department (as the court construed it) and that the rule was "fair and reasonable" because the taxpayer "suffers no hardship" by it, as the commissions paid in purchasing the securities may be deducted when the securi-

ties are eventually sold. But these reasons are wholly inapplicable in the instant case. Unless the commissions are deductible as expenses there is a *certainty* of hardship suffered here and not a mere "hazard" as suggested on page 7 of the petition. The court below pointed out that the commissions in issue were paid on shares sold at a loss (R. 71) and said (R. 74):

> The taxpayer suffered no hardship by such a rule as was pointed out in Hutton v. Commr., 39 Fed. 2, 459 (C. C. A. 5), since under the Revenue Acts then in force the commissions would be reflected against income when the securities were eventually sold. But under the 1932 Revenue Act, due to section 23 (r), the commissions paid would not be reflected against gross income unless the sale of the securities resulted in a profit.

Because of these fundamental differences between the 1921 and the 1932 Revenue Acts there is no conflict between the *Hutton* case and the decision of the court below in this case.

This fundamental difference between the Revenue Act of 1932 and the prior revenue acts is caused by Section 23 (r) of the Revenue Act of 1932, which was first introduced in the latter Act. In view of this difference, the Revenue Acts of 1918, 1921, 1924, 1926, 1928 and 1932 cannot be regarded as having given legislative approval to the former regulations as applied to the 1932 Revenue Act, because that Act is so fundamentally different from the earlier acts in the matter of treating deductions for securities losses. It made little or no difference under the earlier acts whether commissions were capitalized or expensed, because they would reduce income in either event. But under the 1932 Act, unless the securities are sold at a profit the commissions can never be deducted if they are not expensed. The rule of legislative approval of department regulations therefore, has no application in the instant case. The wording of the rule as stated in *Brewster* v. *Gage,* 280 U. S. 327,

337, relied upon by the petitioner, demonstrates its own inapplicability. The rule as stated there is:

> The *substantial re-enactment* in later acts of the provision theretofore construed by the Department is persuasive evidence of legislative approval of the regulation. (Emphasis ours)

The rule as stated in *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 466, and relied upon by the petitioner, also illustrates the point that a "material change" in a subsequent statute destroys, as to that Act, the application of regulations theretofore deemed to have legislative approval. The rule as stated there is:

> The administrative construction must be deemed to have received legislative approval by the re-enactment of the statutory provision, *without material change.* (Emphasis ours)

Conclusion.

The decision of the Circuit Court of Appeals is correct. There is no conflict of authorities and the decision below is fully supported by the facts and by the law. The petition for certiorari should therefore be denied.

Respectfully submitted,

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March 31, 1938.

FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

No. 11.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

ROBERT C. WINMILL, *Respondent*.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF FOR THE RESPONDENT.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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BRIEF FOR THE RESPONDENT.

Opinions Below.

The opinion and dissenting opinion of the Board of Tax Appeals (R. 8-16) are reported in 35 B. T. A. 804. The opinion of the United States Circuit Court of Appeals for the Second Circuit is reported in 93 Fed. (2nd) 494.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered December 13, 1937. (R. 38-39) The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

Whether respondent who is engaged in the business of buying and selling securities for his own account may, in determining his taxable income, deduct buying commissions in the amount of $7493.50, paid to brokers in the purchase of securities both bought and sold during the taxable year.

Statement.

In the year 1932 respondent operated three separate security trading accounts. (R. 9) During that year he sold 61,992 shares of stock through the said three accounts, the cost of which to respondent was $2,884,531.14 (R. 9) exclusive of purchase commissions which amounted to $8,911, of which $7,493.50 was paid by respondent in 1932. The 61,992 shares were sold by respondent in 1932 for $2,722,904.37, on which selling commissions were paid by respondent during 1932 in the amount of $9,574. (R. 10) The operation of these three security accounts resulted in a loss of $161,626.77 not including commissions.

At the end of the year 1932 respondent had on hand in his individual trading accounts shares of stock on which purchase commissions in the amount of $403 had been paid by him during that year. This amount is not included in the purchase commissions above described. (R. 10)

During the year 1932 respondent operated four joint stock trading accounts in which persons other than he had an interest and in which stocks and bonds were bought and sold for profit. Respondent's share in this said profit amounted to $2,267.80. None of the shares sold through any of the above seven accounts were held for two years or more. (R. 10)

In his return for the year 1932 respondent claimed a deduction (on line 8, R. 32) of $172,771.02 as losses on the sale of stocks made up as follows (See Schedule, R. 31):

Cost of stock sold in 1932 through three indivdual accounts	$2,883,773.95
Premiums paid on individual accounts, 1932	395.51
Premiums paid on individual accounts, 1932	361.68
Cost plus premiums on stock sold in 1932 on three individual accounts	$2,884,531.14
Selling price of 61,992 shares sold through three individual accounts	$2,719,760.69
Premiums received on sales through three accounts	1,929.67
Premiums received on sales through three accounts	1,214.01
Selling price, plus premiums received on sales through three accounts	$2,722,904.37
Cost as indicated above	$2,884,531.14
Selling price as indicated above	2,722,904.37
Loss on sales through three individual accounts, including tax but not including commissions	$ 161,626.77
Buying commissions on stock sold in 1932, through three individual accounts	8,911.00
Selling commissions on stock sold in 1932, through three individual accounts	9,574.00
Loss on sales through three indivdual accounts, including tax and commissions	$ 180,111.77
Tax paid in 1932 on 1932 sales through three individual accounts.	5,072.95
Loss on sales through three indivdual accounts including commissions but not tax (taxes claimed and allowed as deductions)	$ 175,038.82
Gain on sales through four joint stock trading accounts attributable to respondent's interest	2,267.80
Net loss claimed on 1932 return on account of three individual accounts and four joint-stock trading account	$ 172,771.02

In the said return for the year 1932 respondent included as income "Interest on Bank Deposits, Notes Corporation Bonds, etc.. (except interest on tax-free covenant bonds)" in the amount of $29,876.34. Respondent also included as "Income from Partnerships, Syndicates, Pools etc.", $27,-984.15 described as "Gude, Winmill Co., 1 Wall St., N. Y." and "Dividends on Stock of Domestic Corporations", $11,-785, thus resulting in a total loss of $103,125.53. Respondent claimed as deductions in the return "Taxes Paid" in the amount of $10,860.86 and "Other Deductions Not Reported Above", described as "Capital Loss held over 2

years'', $22,560.05. The total loss reflected in respondent's return amounts to $136,546.44. (R. 32)

In the audit of the said return the Commissioner, relying on Section 23(r)(1) of the Revenue Act of 1932, added to respondent's income $175,018.67, explained as follows (R. 7):

Stock profit joint accounts	$	2,247.65
Stock losses		172,771.02
Total	$	175,018.67

The Commissioner thus disallowed the claimed deduction from the three separate security accounts in the amount of $161,626.77, and disallowed buying commissions in the amount of $8,911 and selling commissions in the amount of $9,574. The Commissioner also added to respondent's income the $2,247.65 "Stock Profit Joint Accounts" (included in respondent's income as the amount $2,267.80, R. 31). The Commissioner also adjusted the partnership income of $27,984.15 by decreasing such income to the extent of $8,473.06. These adjustments resulted in a deficiency in income tax for the year 1932 for respondent in the amount of $5,508.14.

Respondent contended before the Board that the $7,493.50 representing purchase commissions on securities bought and sold during 1932 and the $403 representing purchase commissions on securities bought but not sold during 1932, and the selling commissions on securities sold during 1932 in the amount of $9,574 were deductible under Section 23(a) of the Revenue Act of 1932 as ordinary and necessary expenses of carrying on the business of buying and selling securities during 1932. (R. 13, 14, 16-23) Respondent also contended that the effect of the disallowance of stock losses under Section 23(r) of the Revenue Act of 1932 resulted in the taxation of receipts not constituting income in the sense intended by the Sixteenth Amendment to the Constitution, and, therefore, that section was void as imposing a direct unapportioned tax in violation of the pro-

visions or Article I of the Constitution (R. 11, 16-23), and that the application of this limitation only to traders in stocks and bonds constituted a discrimination prohibited by the due process provisions of the Fifth Amendment to the Constitution. (R. 11, 16-23)

Respondent also argued before the Board that the $2,-247.65 item described by the Commissioner as "Stock Profit Joint Accounts" constituted respondent's individual profit from sales of stocks and bonds and was properly to be offset against respondent's losses from sales of stocks and bonds. The United States Board of Tax Appeals affirmed the Commissioner of Internal Revenue on all grounds (R. 8-15, 23), Members Arundell, Leech, Arnold, Harron and Black dissenting (R. 15, 16), affirming the addition to income of $2,247.65 described as "Stock Profit Joint Accounts" on the ground that this gain reached respondent through *joint* ventures in which others were also interested and was partnership gain as distinguished from respondent's *individual* gain in such a sense as not to be offset under Section 23(r)(1) of the Act against respondent's *individual* stock losses. (R. 12) The Board made no finding, however, as to whether respondent was engaged in the business of buying and selling securities in 1932 since it believed that in any event the commissions were not deductible. (R. 12-14)

The Circuit Court of Appeals sustained the Board on all grounds (R. 35-37) except as to commissions in the amount of $17,067.50 (R. 37, 38) ($7,493.50 plus $9,574, R. 35), no mention being made by the court of the $403 representing commissions paid on securities bought but not sold during 1932. In its opinion the Circuit Court of Appeals held that commissions were business expense and ordered that the case be remanded to the Board for a finding as to whether respondent was engaged in the business of buying and selling securities in 1932. "If so, the commission for purchases and sales are deductible." (R. 38) Earlier in its opinion the court had stated that the evidence would justify

such a finding. (R. 37) The mandate of the Circuit Court of Appeals was not stayed and on December 31, 1937 the Board of Tax Appeals pursuant to the remand found as a fact that respondent was engaged in the business of buying and selling securities in 1932. (Petitioner's brief page 7, Note 1 at bottom of page)

The petition for certiorari sought a review of the decision only insofar as it related to the commissions paid by respondent on the purchase of shares of stock in the amount of $7,493.50 on the three separate trading accounts and as to buying commissions in the amount of $270 paid by respondent in connection with four security trading accounts jointly operated with others. (Petition page 3)

Summary of Argument.

The United States Circuit Court of Appeals in allowing respondent to deduct brokerage commissions paid on the purchase of securities in the amount of $7,493.50, incident to a trade or business, correctly regarded such commissions as ordinary and necessary expenses in the form of compensation for personal services actually rendered under Section 23(a) of the Revenue Act of 1932.

The purchase commissions in the amount of $270 paid by respondent in connection with certain transactions executed jointly with others are allowable in any event inasmuch as this trading resulted in a profit. This point as to the $270 purchase commissions was not raised by petitioner before the Board or the Circuit Court and may not be raised for the first time here.

In the alternative, respondent contends that if this court should hold that the 1932 act must be construed to require that the commissions of $7,493.50 should be added to the cost of respondent's stocks and bonds sold during 1932, and increase, to that extent, the loss already disallowed under the limitation provisions of Section 23(r)(1) of the Revenue Act of 1932; then respondent urges, in support of the

judgment allowing such commissions as a deduction, that to the extent that the provisions of Section 23(r)(1) of the said Act are to be construed as disallowing these commissions, such provisions are unconstitutional and void under Article I, Section 2, Clause 3 and Article I, Section 9, Clause 4 of the Constitution of the United States for the reason that such construction of the Act has the effect of levying a direct unapportioned tax on subject matter or property not contemplated by the word "incomes" within the meaning of the Sixteenth Amendment to the Constitution, because that word as used in the Sixteenth Amendment was understood by its framers and the people who ratified it to refer to the "computation of income annually as the *net result of all transactions within the year*, (see *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, 365), and, further, that the said provisions of Section 23(r) are unconstitutional and void to the extent that they disallow the said $7,493.50, because they are arbitrary, capricious and whimsical, and, therefore, violate the due process clause of the Fifth Amendment to the Constitution, resulting in the imposition of a tax at progressive rates on gross receipts, improperly discriminating between persons without reference to their ability to pay, although the supposed reasonable ground for proper discrimination arising from progressive surtax rates, is their relative ability to pay.

These latter arguments are made merely to sustain affirmance of the decision of the court below.

STATUTE AND REGULATIONS INVOLVED.

Excerpts from the Revenue Act of 1932.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *.

* * * *

(e) *Losses by Individuals.*—Subject to the limitations provided in subsection (r) of this section, in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; * * *.

* * * *

(r) *Limitation on stock losses.*—

(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

* * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b), and the loss shall be the excess of such basis over the amount realized.

* * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (unadjusted) of property.*—The basis of property shall be the cost of such property; * * *

* * * * *

(b) *Adjusted basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) *General rule.*—Proper adjustment in respect of the property shall in all cases be made—

(A) for expenditures, receipts, losses, or other items, properly chargeable to capital account, including taxes and other carrying charges on unimproved and unproductive real property, but no such adjustment shall be made for taxes or other carrying charges for which deductions have been taken by the taxpayer in determining net income for the taxable year or prior taxable years;

REGULATIONS.

Excerpts from Regulations 77 relating to the Revenue Act of 1932:

ART. 103. *Inventories at cost.*—Cost means:

* * * * * *

(2) In the case of merchandise purchased since the beginning of the taxable year, the invoice price less trade or other discounts, except strictly cash discounts approximating a fair interest rate, which may be deducted or not at the option of the taxpayer, provided a consistent course is followed. To this net invoice price should be added transportation or other necessary charges incurred in acquiring possession of the goods.

ART. 121. *Business expenses.*—Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except the classes of items

which are deductible under the provisions of articles 141-272. The cost of goods purchased for resale, with proper adjustment for opening and closing inventories, is deducted from gross sales in computing gross income. (See article 55). Among the items included in business expenses are management expenses, *commissions*, labor, supplies, incidental repairs, operating expenses of automobiles used in the trade or business, traveling expenses while away from home solely in the pursuit of a trade or business (see article 122), advertising and other selling expenses, together with insurance premiums against fire, storm, theft, accident, or other similar losses in the case of a business, and rental for the use of business property. A taxpayer is entitled to deduct the necessary expenses paid in carrying on his business from his gross income from whatever source. As to items not deductible, see section 24 and articles 281-284. (Emphasis ours)

Art. 282. *Capital expenditures.*—Amounts paid for increasing the capital value or for making good the depreciation (for which a deduction has been made) of property are not deductible from gross income. (See section 23(k) and article 201) Amounts expended for securing a copyright and plates, which remain the property of the person making the payments, are investments of capital. The cost of defending or perfecting title to property constitutes a part of the cost of the property and is not a deductible expense. The amount expended for architects' services is part of the cost of the building. Commissions paid in purchasing securities are a part of the cost of such securities. Commissions paid in selling securities, when such commissions are not an ordinary and necessary business expense, are an offset against the selling price * * *.

Argument.

I.

In this proceeding the only question properly before this Court is the deductibility of brokerage commissions in the amount of $7,493.50 on securities bought and sold during the year in respondent's three individual trading accounts.

At the outset it should be pointed out that the petition for certiorari sought review only as to the following specific question or matter upon which the lower court ruled:

> (1) Deductibility of brokerage commissions in the purchase of securities in the sum of $7,493.50 on the three separate trading accounts which respondent operated individually during 1932. (Petition p. 3)

The petition also sought review as to the following point or question:

> (2) Deductibility of brokerage commissions in the purchase of securities in the sum of $270 on the four security trading accounts which respondent operated jointly with other persons. (Petition p. 3)

Inasmuch as this latter point or question was not raised in this proceeding before the Board of Tax Appeals or before the Circuit Court of Appeals below, it cannot be raised by petitioner for the first time upon certiorari in this court. *Helvering* v. *Minnesota Tea Company*, 296 U. S. 378, 380, 56 S. Ct. 269, 270.

The petition for certiorari did not seek review as to any other point or matter upon which the Board of Tax Appeals or the United States Circuit Court of Appeals below ruled on. Specifically, the petition did not seek review as to the deductibility of purchase commissions in the amount of $403 which were paid on securities purchased in 1932 by respondent through his own three individual trading accounts.

The petitioner at page 7 of his brief is attempting to make it appear that the petition for certiorari embraced the question of the deductibility of the commissions in the amount of $403 which the petition actually omitted. The attempt is made to make it appear to this court that the petition sought review as to a total or lump sum, namely "$7,896.56" which petitioner explains as being "$7,493.50 plus $403". In note 2 at the bottom of page 7 of petitioner's brief it is asserted that:

> "The petition (p. 3) erroneously gives the total as $7,763.50 ($7,493.50 plus $270)."

Quite on the contrary, neither total figure was used in the petition. Two separate amounts were given with definite references to pages in the record in the court below: "$7,493.50 (R. 20)" and "$270 (R. 20)".

In the record of the court below the $403 item appears on a different page, namely page 21. (R. 10) The $270 amount according to the petition expressly refers to commissions involved in "four securities trading accounts" which respondent "operated jointly with others"; whereas those commissions are entirely different from the purchase commissions in the sum of $403, which respondent had paid in 1932 on securities on hand at the end of the year in his own "three individual trading accounts". (R. 10)

From the foregoing it is clear that the question of the action of the Circuit Court of Appeals with respect to these latter commissions ($403) was not presented by the petition for certiorari and may not be considered here. *Steel* v. *Drummond*, 275 U. S. 199, 48 S. Ct. 53; *Johnston* v. *Manhattan R. Co.*, 289 U. S. 479, 53 S. Ct. 721; *Olson* v. *United States*, 292 U. S. 246, 54 S. Ct. 704; *Prudence Company, Inc.* v. *Fidelity and Deposit Co.*, 297 U. S. 198, 56 S. Ct. 387.

For the foregoing reasons respondent will confine his brief only to a discussion of matters relating to the deductibility of brokerage commissions in the amount of $7,493.50. Inasmuch as these commissions were all paid with

respect to securities both bought and sold by respondent during the year 1932, the rule laid down by the United States Circuit Court of Appeals for the Fifth Circuit in the case of *Hutton* v. *Commissioner*, 39 Fed. (2d) 459, under the 1921 Revenue Act (42 Stat. 237) is clearly inapplicable, inasmuch as the commissions there were commissions paid on stocks bought during the year but not disposed of until a later year under a regulation which allowed them to be deducted in such later year. For this reason, as will be more particularly discussed below (pages 23-24 this brief), there is no conflict between the decision of the court below and the *Hutton case* or any other case cited by petitioner and if this court granted certiorari on the ground of such a conflict, it is respectfully urged now that the writ was improvidently granted. This contention was also urged by respondent in his brief in opposition to the petition.

II.

Compensation paid brokers for services rendered in connection with the purchase and sale of stocks in the course of the ordinary and necessary operations of a taxpayer's trade or business is deductible under Section 23 (a).

Section 23(a) of the Revenue Act of 1932 provides that there *SHALL* be deducted in computing net income, the ordinary and necessary expenses of carrying on any trade or business "*including a reasonable allowance for salaries, or other compensation for personal services actually rendered* * * *." (Emphasis ours)

Commissions paid to brokers for effecting the purchase and sale of stocks in the course of a business, constitute "compensation for personal services actually rendered", and are, therefore, deductible under the above statute. "A merchant employing a buyer on salary would unquestionably deduct the salary as current business expense rather than allocate it as part of the cost of goods, and in sub-

stance a commission paid to a buyer is not different". Arundell's dissenting opinion, *Winmill* v. *Commissioner*, 35 B. T. A. 804, 810 (R. 15-16)

The statute, Section 23(a), creates the classification of "compensation for personal services actually rendered", and provides that such "compensation" is deductible as an expense. The *statute* mentions no more specific classification than such "compensation". The *regulations* (Article 282) create the more specific classification, or sub-classification, of compensation, namely "commissions paid in purchasing securities", and provide inconsistently with the statute that such commissions are to be capital expenditures as distinguished from ordinary and necessary expenses. This inconsistent treatment in the regulations, of the statutory classification of "compensation" is unwarranted, unless the classification of "commissions paid in purchasing securities" is justified under the more *general* statutory treatment (Section 113(b)(1)(A)) of "items, properly chargeable to capital account". But in determining whether it was the intent of Congress to govern "commissions paid in purchasing securities" by the general statutory classification, "items, properly chargeable to capital account", or by the more specific statutory classification, "compensation", the general statutory treatment of "items, properly chargeable to capital account" must yield to the more specific statutory treatment of "compensation", because we are dealing with "compensation for personal services actually rendered" in the form of commissions.

Obviously, the Commissioner is attempting, contrary to the statute, to regulate the statutory classification of "compensation" without reference to whether or not such compensation in true substance qualifies under the broader statutory phrase "items, properly chargeable to capital account"; that is to say, the Commissioner here contends that his regulations mean that *all* "commissions paid in purchasing securities" are to be capitalized and not expensed, irrespective of their being statutory compensation and re-

gardless of whether or not they are statutory "items, properly chargeable to capital account".

The words, "items, properly chargeable to capital account" have been held to include only such items as are not specifically named as deductible expenses in the statute but which are paid for increasing capital value. See *Central Real Estate Company v. Commissioner*, 47 Fed. (2d) 1036 where the United States Circuit Court of Appeals for the Fifth Circuit decided that interest and taxes paid with respect to unproductive property could not be added to the cost of such property (for the purpose of determining the gain or loss from its sale), as amounts "properly chargeable to capital account". Speaking for the Court in that case as to the meaning of the quoted phrase, Circuit Judge Foster said that it "clearly contemplated only such items as add to the value of the property". He then added:

> "If Congress had intended to give the taxpayer the privilege of adding taxes and interest to cost, it would have been very easy to have said so. As the act does not so provide, the conclusion is inescapable that Congress did not so intend."

That case was decided in 1931 under Section 202(b) of the Revenue Act of 1924 (26 U. S. C. A. §933, note), under which proper adjustment was to be made for any expenditure "properly chargeable to capital account". The words "including taxes and other carrying charges on unimproved and unproductive real property" were not included in the 1924 Act (26 U. S. C. A. §933, note), but appear *for the first time* in the 1932 Act in Section 113(b)(1)(A), which corresponds to Section 202(b) of the 1924 Act. Nor were these added words in the corresponding provisions of the Revenue Act of 1926 (26 U. S. C. A. §933) or 1928 (26 U. S. C. A. §2111). They were undoubtedly added to the law in 1932 to change the law as interpreted by the Fifth Circuit. If Congress had intended compensation in the form of commissions to be included in the phrase "prop-

erly chargeable to capital account", the words "commissions paid in purchasing securities" would undoubtedly have been added to Section 113(b)(1)(A) of the 1932 Act, because of the inclusion in Section 23(a) of "compensation for personal services actually rendered". See also *Westerfield* v. *Rafferty*, 4 Fed. (2d) 590 (D. C., E. D. N. Y.); *Fraser* v. *Commissioner*, 25 Fed. (2d) 653 (C. C. A. 2); *H. M. O. Lumber Co.* v. *United States*, 59 Fed. (2d) 907. Under this theory "finance charges" were held by the Court of Claims in *Moran* v. *U. S.*, 19 Fed. Supp. 557, as being correctly regarded as "expenses" rather than as "items properly chargeable to capital account".

Furthermore, the Commissioner's own regulations, Article 282 at the very outset define "capital expenditures" as "amounts paid for increasing capital value". "Commissions paid in purchasing securities" add nothing to the value of the securities purchased. Securities purchased directly without commissions are worth no less than the identical securities purchased through a broker to whom commissions are paid. Commissions, therefore, add nothing to the value of the asset involved, nor do the commissions here constitute "amounts paid for increasing capital value".

The recognized accounting authorities in dealing with the subject of amounts properly chargeable to capital account, invariably illustrate their texts with references to items which are clearly of a capital nature, such as buildings, machinery, and bonds purchased for a permanent investment. See Kester: Accounting—Theory and Practice, Volume 1 (3rd revised edition) page 516. None of the illustrations refer to securities bought and sold in the course of a *trade or business*. Kester, Volume 1 (3rd revised edition) page 517 treats the problem of amounts properly chargeable to capital account with respect to temporary investments of funds idle for the time being. Obviously these illustrations are also to be distinguished from securities purchased and sold by a trader such as Mr. Winmill.

was, because his securities are in the nature of inventory or merchandise items. From an accounting standpoint, therefore, it is clear that the words "properly chargeable to capital account" mean just what they say, with particular emphasis on "capital account". Bonds held for investment, annuities held for income purposes, buildings, plant equipment and the like are items that would normally go in the *capital account;* while merchandise purchased for resale in the course of business would be carried in the merchandise account as distinguished from the capital account, and a person engaged in the business of trading or buying and selling property would account for his purchases in an account comparable to the merchandise account as distinquished from his capital account. Thus, a trader in securities would not be required by the phrase "properly chargeable to *capital account*" to add his buying commissions to such an account. Buying commissions are analogous to buyers' salaries, and need not be allocated to cost of goods. The fact that they may easily be so allocated does not make it necessary to do so nor does it require the provisions of Section 23(a) to be ignored.

It has been the long established custom of the Bureau of Internal Revenue to allow buying and selling commissions as deductions when such commissions are paid with respect to property bought and sold in the course of a trade or business of the taxpayer. This practice is evidenced by the Commissioner's published ruling which is still in force, namely, I. T. 2305 published on page 108 of Cumulative Bulletin V-2. This ruling reads as follows:

> "In the case of sales of real estate by persons not regularly engaged in that business, commissions paid, while they do not reduce or otherwise affect the amount of the selling price, may be offset against the selling price in determining the amount of gain or loss realized from such sales, and in cases of installment sales in determining the percentage of profit in each installment payment which is to be included in gross income.
>
> "Dealers in real estate should deduct commissions

paid for the sale of real estate as a business expense for the year in which paid or accrued, in accordance with the basis on which their books are kept."

The allowance of commissions on real estate sales as a business expense was approved by the Board of Tax Appeals in the *Highlands Trust*, No. 1546, 32 B. T. A. 760, expressly on the authority of I. T. 2305 quoted above. In that case the taxpayer was seeking to add commissions to the cost of real estate sold during the year. This the Board refused to do saying at page 766:

"We gather from statements in the deficiency notice and the briefs of the parties that the respondent treated the commission retained by the Paramount Realty Corporation as a deductible business expense rather than as a reduction of either the selling price of the lots or the initial payment thereon. This is in accordance with the long established practice of the Bureau. See I. T. 2305, C. B. V-2, P. 108; art. 352, Regulations 74 and 77; art. 44-2, Regulations 86. Petitioners' claim, as we understand it, is that the net amount received after deducting the part retained by the Paramount Realty Corporation should be treated as the selling price. This would have the effect of throwing back into the earlier years some of the profit ultimately realized on the deferred payment sales. We know of no authority for this method of computing income. The gross amount which purchasers contracted to pay was the selling price and must be accounted for as such, regardless of bookkeeping or accounting methods. *Commissions on sales are business expenses to be deducted in the years of accrual or payment, according to whether the taxpayer is on the accrual or cash basis, and are to be deducted in arriving at net income.* This is the normal method of determining income and petitions have not shown any reason for a departure therefrom. Some argument is made as to the lack of value of the sales contracts. We do not see what this has to do with the question presented; moreover, there is no evidence at all as to the value of the contracts." (Emphasis ours)

See also *Clarence Whitman* v. *Commissioner*, 16 B. T. A. 197, 199, affirmed by this Court, 49 Fed. (2d) 1087; *Alexander Sprunt & Son* v. *Comm.*, 64 Fed. (2d) 424, 428 and *Kornhauser* v. *U. S.*, 276 U. S. 145.

The principle is equally applicable to one whose trade or business involves the purchase and sale of stocks for a profit. The buying and selling commissions constitute "compensation for personal services actually rendered", "in carrying on any trade or business", and are clearly deductible.

The Commissioner in his petition does not question the Circuit Court's ruling with respect to *selling* commissions, but only as to purchase commissions. There is no difference in principle between these two classes of commissions and there is no good reason for allowing one and disallowing the other as petitioner contends the Regulations do. The Commissioner's regulations if construed so as to allow one and disallow the other are unreasonable and should be disregarded to the extent that they are inconsistent with Section 23(a).

On page 13 of petitioner's brief, after citing in support of his position the case of *Bonwit Teller & Company* v. *Commissioner*, 53 Fed. (2d) 381, in which commissions paid to secure a 21 year lease were held to be capital expenditures deductible ratably over the life of the lease, after pointing out that the court likened such commissions to a fee paid to a broker for negotiating an annuity contract, petitioner says:

> "There appears to be no essential difference between a brokerage fee paid in the acquisition of an annuity contract and one paid in the acquisition of securities."

We believe that there would be little, if any, difference between a brokerage fee paid in the acquisition of an annuity contract and one paid in the acquisition of securities purchased as a *permanent* or *quasi permanent* investment, but when, as here, the commissions are paid in the acquisition of

securities purchased for resale by petitioner in the conduct of a trade or business of buying and selling securities, and when, as here, the securities involved in the issue were all bought and sold during the year 1932, there is no similarity between the commissions paid thereon and the amount of commissions paid in purchasing a long-term annuity, or to commissions paid to secure a lease as in the *Bonwit Teller case* with a term running for 21 years.

In the case of *Helvering* v. *Union Pacific Railroad Company,* 293 U. S. 282, referred to in petitioner's brief (pp. 11, 12), the issue involved the deduction of commissions on bonds issued by the taxpayer itself. Each of the cases cited in the margin of that case by this court in support of its tacit approval of the regulations providing for the capitalization of commissions, involved a commission paid on a clearly *capital transaction* such as a commission on the sale of capital stock being originally issued by the corporation taxpayer.

In that case this court indicated, (see 293 U. S. 282, 286, 287), as did the Circuit Court of Appeals in the *Hutton case,* that the taxpayer suffered no hardship by such a rule because the commission would be reflected against income when the securities were eventually retired or sold. The same lack of hardship is obvious in every single case relied upon by the petitioner. See *Helvering* v. *Union Pacific Co.,* 293 U. S. 282; *Bonwit Teller & Co.* v. *Commissioner,* 53 Fed. (2d) 381 (C. C. A. 2d), certiorari denied, 284 U. S. 690; *Spinks Realty Co.* v. *Burnet,* 62 Fed. (2d) 860 (App. D. C.), certiorari denied, 290 U. S. 636; *Hutchings* v. *Burnet,* 58 Fed. (2d) 514 (App. D. C.); *Commissioner* v. *Chicago Dock & Canal Co.,* 84 Fed. (2d) 288 (C. C. A. 7th); *Beneficial Industrial Loan Corp.* v. *Handy,* 92 Fed. (2d) 74 (C. C. A. 3rd), affirming 16 Fed. Supp. 110 (Del.); *Houston Natural Gas Corp.* v. *Commissioner,* 90 Fed. (2d) 814 (C. C. A. 4th), certiorari denied, 302 U. S. 722; *Baltimore & Ohio R. Co.* v. *Commissioner,* 78 Fed. (2d) 460, 463 (C. C. A. 4th); *Moynier* v. *Welch,* 97 Fed. (2d) 471 (C. C. A. 9th).

In none of these cases could the provision of prior law corresponding to Section 23(a) have been applicable, because the commissions involved were not paid in connection with the purchase and sale of property in the operation of a trade or business.

Neither these cases nor the regulations relied on by petitioner have any application to the case of commissions expended by one carrying on the trade or business of buying and selling securities.

The commissions and other expenses paid in those cases were related to essentially capital matters or were expenditures for property of a more or less permanent nature. They related to property or benefits which lasted in most cases for many years after the expenditure had been made. On the contrary, the commissions here involved were all paid in purchasing securities in the course of respondent's trade or business, all of which securities had been sold in the course of such business before the end of the year.

Even if we assume that the regulations and the decisions cited by the petitioner under laws *prior* to the 1932 act clearly prevented the deduction of commissions paid for services rendered in connection with the purchase and sale of securities in the course of the operation of a trade or business, these former regulations and decisions so holding could not be applicable under the 1932 law, because of the fundamental change effected by Section 23(r)(1).

It is true that legislative re-enactment of a statute *without change* operates as an implied legislative approval of the construction given to the statute before re-enactment, but where, as in the instant case, the statute is re-enacted with a *substantial change* which eliminates the application of a uniformly expressed ground for the previous construction, such previous construction cannot apply to the subsequent dissimilar enactment.

In *DeGanay* v. *Lederer*, 239 Fed. 568, 571, affirmed by the Supreme Court of the United States in 250 U. S. 376, the lower court said:

"Legislative constructions of prior acts have all the value of expressions of opinion by those to whose opinions weight and importance is attached. Inasmuch, however, as such an opinion is that of an autocrat who can impose his will by changing the law, the distinction must always be observed between an opinion of what the law has been and a new enactment. If such subsequent statute gives to the prior one a meaning different from its sound meaning as judicially construed, the latter statute is a new enactment, no matter what its form."

See "Statutes" 59 Corpus Juris 1063 and 1064 indicating clearly that where the old and new statutes are essentially dissimilar, the rule that the construction placed on a former statute by the courts is impliedly adopted by the legislature when it re-enacts such statute, or enacts analogous legislation, does not apply.

Inasmuch as the regulations and decisions relied upon by the petitioner in support of his position all clearly contemplate the *eventual allowance against income* of the commissions paid in connection with capital purchases and sales, and as the court decisions cited predicate their holding on the premise of *eventual allowance against income*, the said regulations and decisions are not authority to *completely* and *forever disallow* this compensation paid in the operation of a trade or business, contrary to the plain language of Section 23(a).

The words "compensation for personal services" as used in Section 23(a) of the Revenue Act of 1932 are presumed to be used in their ordinary and usual sense and with the meaning commonly attributable to them.

"Unless the contrary appears, statutory words are presumed to be used in their ordinary and usual sense, and with the meaning commonly attributed to them." *DeGaney* v. *Lederer*, 250 U. S. 376 381.

In that sense and with that commonly attributable meaning, the words of Section 23(a) include compensation in the

form of broker's commissions and when such compensation is paid in connection with the purchase and sale of stocks bought and sold in the course of the ordinary and necessary operations of a taxpayer's trade or business, the statute requires that said compensation for services actually rendered *"SHALL"* be allowed as a deduction in computing income.

Petitioner argues (p. 16) that there is no reason to suppose that Congress simply by changing the *consequences* of the classification of an expense as a capital outlay, intended to modify the established classification itself.

The only court case called to respondent's attention which approves the classification under the earlier regulations is *Hutton* v. *Commissioner*, 39 Fed. (2d) 459 (C. C. A. 5) and it is significant that the court's approval thereof was *expressly* justified upon the very *consequences* of which petitioner speaks. Circuit Judge Foster in speaking for the court there said as to the classification:

> "The rule is fair and reasonable. It is clear that the taxpayer suffers no hardship by the rule, as the commission paid in purchasing the securities may be deducted from the profits or added to the losses when the securities are eventually sold." (39 Fed. (2d) 460)

To require the addition of such commissions to one's losses, when it is positive that such resulting loss will not be offset against other actual income, and the result will be that a substantial tax must be paid, which could not arise if the commissions were deductible as an *expense*, certainly constitutes a definite hardship. For this reason, therefore, the above quoted statement certainly cannot be construed as intending under the court's rule, that the losses including the commissions are to be disallowed in any event "when the securities are eventually sold".

But this taxpayer *does* suffer a hardship by application of the former rule in this case, and unless the securities, in the amount of $7,493.50, are to be deducted in 1932, the year

in which the securities were both bought and sold, respondent will never be able to deduct this out-of-pocket expense, which he incurred, in good faith, in the operation of a business, in which he was attempting to produce taxable income. If the commissions are disallowed, respondent will be required to pay a substantial tax even though his losses from these transactions exceeded his gains and income from all sources for the year. However, if the commissions are allowed as a deduction, his taxes for the year will be reduced accordingly.

There is no question of a "possibility" of a "hazard" in this case, as the petitioner terms the possibility (p. 17) that the Commissioner's capital classification rule does not always produce a hardship. In this regard he says the taxpayer may not always have other income to offset such an expenditure. But respondent answers—neither would he pay any tax. In any event, however, it is improper to discuss suppositions inconsistent with the facts here. This respondent *had* other income here, and it is *definitely certain*, in this proceeding, that he *will* suffer a hardship by the application to the new law of the regulations applicable to the former law.

In the light of the unfairness of the definite hardship which would be imposed upon respondent through the disallowance of the deduction for the commissions here in issue, the application to the facts here to the test of fairness and lack of hardship, upon which Circuit Judge Foster's opinion in the *Hutton case* was predicated, would lead inescapably to the allowance of the commissions as expenses. Therefore there is no conflict between that decision and the decision of the Circuit Court in this proceeding.

It is perhaps not without significance that Circuit Judge Foster in rendering the opinion of the court in *Central Real Estate Co.* v. *Commissioner, supra,* refused to permit interest and taxes on unproductive property to be capitalized in determining the gain or loss from the sale of the property because interest and taxes were deductible as an ex-

pense under the Act. In view of this decision, which was rendered just a little less than a year after the decision of the same court in the *Hutton case*, it may be assumed that the Fifth Circuit has now modified its view formerly expressed in the *Hutton case*.

The Commissioner's Regulations, Article 282 specifically recognize that commissions paid in selling securities may sometimes represent an ordinary and necessary expense of doing business by the following provision in that Article:

> "Commissions paid in selling securities, *when such commissions are not an ordinary and necessary business expense*, are an offset against the selling price." (Emphasis ours).

The only reasonable inference from this statement is that when such commissions *are* an ordinary and necessary business expense, they are deductible as such. No similar distinction is made in the Regulations, between buying commissions which *are* and buying commissions which are *not* ordinary and necessary business expenses. There is no reason for holding that commissions paid in *selling* securities may be an ordinary and necessary business expense, but that *all* commissions paid in *purchasing* securities are to be capitalized whether or not they constitute ordinary and necessary business expenses. To the extent that Article 282 of the Regulations fails to recognize that commissions paid in purchasing securities which are ordinary and necessary business expenses, may not be deducted as such expenses, the Regulation is contrary to Section 23(a) and is otherwise wholly unreasonable and arbitrary.

Finally, it is significant to consider that the provisions of Section 23(r) limiting losses on stocks, constitute an express limitation only on Section 23(e)—Losses, and not a limitation on Section 23(a)—Expenses, or any other section. Thus is must be presumed that Congress clearly intended not to limit the expenses incident to carrying on the business of trading in stocks (or the expenses of any othar

business) to be limited by Section 23(r). If Congress had intended to extend the limitation of Section 23(r) to expenses provided for in Section 23(a) it would have said so *specifically* and would have provided definite cross references between Section 23(a) and Section 23(r) as it did between Section 23(e) and Section 23(r).

If there is any doubt about this matter, that doubt should be resolved in favor of the taxpayer. The limitation in Section 23(r) should not be *extended* by *implication* to override the specific provisions of Section 23(a). In *Gould v. Gould*, 245 U. S. 151, 38 S. Ct. 53, this court said:

> "In the interpretation of statutes levying taxes it is the established rule not to *extend* their provisions, by *implication, beyond the clear import of the language used*, or to enlarge their operations so as to embrace matters *not specifically pointed out*. In case of doubt they are construed most strongly against the government, and in favor of the citizen." (Emphasis ours)

III.

If the commissions are not deductible as ordinary and necessary expenses, they are deductible as losses under Section 23 (e) (1) of the Revenue Act of 1932.

Even if it should be held by this court that the commissions constitute "items properly chargeable to capital account", the amounts paid, therefore, are expenditures made in good faith to produce taxable income and when the securities upon which they are paid have been disposed of, the taxpayer has nothing left to show for this expenditure. Thus, the amount so expended becomes a loss deductible under Section 23(e)(1) of the Revenue Act of 1932 for losses "if incurred in trade or business". If these commissions are properly to be considered a part of the taxpayers losses, such losses are not "losses from sales or exchanges of stocks and bonds (as defined in sub-section (t) * * *)". The definition of stocks and bonds contained in Section 23 (t) of the Revenue Act of 1932, although very explicit, con-

tains no reference whatsoever to commissions. It must be presumed, therefore, that Congress did not intend to disallow losses to the extent that they represent commissions paid. It would require clear and unequivocal language to hold that commissions were intended to be included by the definition of stocks and bonds in Section 23(t). The definition reads as follows:

> "(t) Definition of Stocks and Bonds.—As used in subsection (r) and (s), the term 'stocks and bonds' means (1) shares of stock in any corporation, or (2) rights to subscribe for or to receive such shares, or (3) bonds, debentures, notes, or certificates or other evidences of indebtedness, issued by any corporation other than a government or political subdivision thereof), with interest coupons or in registered form, or (4) certificates of profit, or of interest in property or accumulations, in any investment trust or similiar organization holding or dealing in any of the instruments mentioned or described in this subsection, regardless of whether or not such investment trust or similar organization constitutes a corporation within the meaning of this Act."

IV.

To the extent that Section 23(r) of the Revenue Act of 1932 may be held by this court to disallow the buying commissions in the amount of $7,493.50, such Section is unconstitutional and, void under Article I, Section 2 Clause 3 and Section 9, Clause 4 of the Constitution, because as so construed the Act levies a direct unapportioned tax on subject matter not contemplated by the word "incomes" within the meaning of the Sixteenth Amendment to the Constitution.

Solely in the alternative and to support the judgment of the court below in allowing the buying commissions in the amount of $7,493.50 to be deducted, respondent contends that if this court should hold that the Revenue Act of 1932 must be construed so as to require that the said purchase

commissions should be added to the cost of respondent's stocks and bonds (held less than two years and sold in 1932) and so increase, to that extent, the large loss already disallowed under the limitation provisions of Section 23(r)(1) of the Revenue Act of 1932, then respondent urges in support of the judgment that to the extent that the provisions of the said section require the disallowance of the said expenditure of $7,493.50, to that extent the Act is unconstitutional and void under Article I, Section 2, Caluse 3 and Article I, Section 9, Clause 4 of the Constitution of the United States, for the reason that so construed, the Act has the effect of levying a direct unapportioned tax upon subject matter or property not contemplated by the word "incomes", within the meaning of that word as used in the Sixteenth Amendment to the Constitution.

Respondent would have filed a cross petition for certiorari as to this issue, but as a computation under the judgment below reflects a deficiency of only about $700.00 and as respondent was absent from the country during the time between the filing of the petition herein and the expiration of the time for filing cross petition, he must content himself with raising the issue only as an alternative and in support of the judgment below. Nothing said herein is intended to be construed as an attack upon that judgment.

Before the adoption of the Sixteenth Amendment to the Constitution, Congress was without practical power to tax incomes, without apportionment according to the population. It was held in the case of *Pollock* v. *Farmers' Loan and Trust Company*, 157 U. S. 429, that an income tax is a direct unapportioned tax and that the imposition of direct unapportioned taxes was specifically prohibited by Article I, Section 2, Clause 3 of the Constitution and because, Article I, Section 9, Clause 4 of the Constitution required that all direct taxes be apportioned according to the population.

By the Sixteenth Amendment, the necessity for apportioning "incomes" was done away with, but the prohibition

in Article I, Section 2, Clause 3 against unapportioned direct taxes not covered by the Sixteenth Amendment remained, as did the requirement of Article I, Section 9, Clause 4 of the Constitution that direct taxes be apportioned.

Thus after the amendment, the necessity for apportionment remained with respect to all direct taxes except whatever the framers of the Constitutional amendment meant by "incomes, from whatever source derived".

The sense in which these words were used constitutionally, in the light of, (a) the history of income taxation, (b) in the light of the events leading up to and the purpose of the adoption of the Sixteenth Amendment, (c) in the light of the retained Constitutional restrictions against other unapportioned direct taxes, and (d) in the light of the Supreme Court's definition of the word "incomes", must be considered in order to know the extent to which direct unapportioned taxes may be constitutionally imposed under the Sixteenth Amendment.

Specifically, the question resolves into this query: does the word "incomes" as used in the Amendment mean, (a) the substantial equivalent of net income in an economic sense, (b) gross receipts, or (c) anything which Congress might choose to call income?

The history of income taxation in the United States reflects the fact that the taxation of incomes, computed annually upon the *net result of all transactions within the year*, was a familiar practice before the adoption of the Amendment, (*Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359), and that the Amendment was adopted to meet the decision of the United States Supreme Court in *Pollock* v. *Farmers' Loan and Trust Company, supra* (declaring the income tax law of August 15, 1894, to be unconstitutional as a direct unapportioned tax), so as to empower Congress to levy a tax like the 1894 income tax law.

This act of 1894 imposed a tax upon the substantial equivalent of net income in an economic sense and com-

puted "incomes" upon the *net result of all transactions within the year.* The definition of income in section 28 of that act included the following formula:

> "In computing *incomes* the necessary expenses actually incurred in carrying on any business, occupation, or profession shall be deducted * * * also *losses actually sustained during the year, incurred in trade.*" (Emphasis ours)

Note that the word "*incomes*" is spelled plurally as it is in the Sixteenth Amendment.

The procedure, under which the Sixteenth Amendment was adopted, was instituted under Article II, Section 3 and Article V of the Constitution, by President Taft's formal message on the State of the Union which he addressed to Congress on June 16, 1909. This message resulted in the joint resolution of the Senate and the House which, upon its ratification by the legislatures of three-fourths of the states, became the Sixteenth Amendment to the Constitution. At the time of this message there was pending in Congress a bill for the imposition of a tax upon the substantial equivalent of net income in an economic sense, which provided that "incomes" should be computed *upon the net result of all transactions within the year.*

The President's message requesting the adoption of a Constitutional amendment, which would give Congress the power to impose taxes upon incomes, without apportionment stated that there was then pending in Congress a bill for the collection of:

> "a general income tax, in form and substance of almost exactly the same character as that which in the case of *Pollock v. Farmer's Loan & Trust Company* (157 U. S. 429) was held by the Supreme Court to be a direct tax, and therefore not within the power of the Federal Government to impose unless apportioned among the several States according to population."

After pointing out that he believed that the National Government ought to have such power the President's message continued,

> "I therefore recommend to the Congress that both houses, by a two-thirds vote, shall propose an amendment to the Constitution conferring the power to levy an income tax upon the National Government without apportionment, among the States in proportion to population.
>
> * * * I have become convinced that a great majority of the people of this country are in favor of vesting the National Government with power to levy an income tax, and that they will secure the adoption of the amendment in the States if proposed to them."

The bill referred to by President Taft in his message was H. R. 110 (61st Congress, First Session). This bill was introduced by Representative Cordell Hull of Tennessee on March 15, 1909. This bill, like the Revenue Act of 1894, provided an income tax upon the *net result of all transactions within the year*. Section 2 of that bill provided that:

> "In computing incomes the necessary expenses actually incurred in carrying on any business, occupation, or profession shall be deducted, * * * also *losses actually sustained during the year, incurred in trade* * * *." (Emphasis ours.)

This bill failed of passage probably because it was believed that it would be declared unconstitutional as in the case of the 1894 Act.

Thus it is clear that the scheme of taxation which the proponents of the Amendment wished Congress to be empowered to enact, was a tax upon the substantial equivalent of net income in an economic sense computed upon the basis of the net result of all transactions within the year. During the debates there was continually held up to Congress the 1894 law as the specific pattern to illustrate the sort of power which was desired.

All through these discussions of the proposed amendment, it was indicated that the power sought to be delegated was the power to impose a *net* income tax. References to the "net income tax" (Cong. Rec. Vol. 44, p. 4393), the "fairness" of the income tax (Cong. Rec., Vol. 44, p. 4392), and to the "equity of an income tax" (Cong. Rec., Vol. 44, p. 4398), indicate that the familiar *net* income tax as then understood was all that was wanted.

Representative Champ Clark of Missouri said:

> "My own judgment is that the wit of man never devised a fairer or juster tax than a graduated income tax." (Cong. Rec., Vol. 44, page 4392.)

He further said (at page 4393):

> "But I say that when a man's *net* income rises above \$100,000 a year it does not make any difference to him, practically, whether you *take* one per cent., two per cent., five per cent., or twenty-five per cent. as they do in Germany." (Emphasis ours.)

Representative De Armond in explaining his vote for the Amendment Resolution said: "There is no good reason why taxation should not be *according to ability to pay*." (Emphasis ours.) (Cong. Rec., Vol. 44 top of page 4420.)

Representative Hobson said: "Taxes upon incomes represent the least burdensome of all taxes on wealth, and the burdens decrease with the size of the income." (Cong. Rec. Vol. 44 p. 4430.)

All the discussions centered around getting a delegation of power to pass a *net* income tax like the Act of 1894. The constant fear was expressed that the ratification by the necessary three-fourths of the States might fail due to opposition. (Cong. Rec. Vol. 44, p. 4419.) A bitter controversy did arise concerning its ratification (Cong. Rec. Vol. 44, p. 1694) and the States took longer to ratify that amendment than any other amendment except the Eleventh which was ratified one hundred and fifteen years before. If it had

been publicly understood while ratification was pending that the power sought, included the power to tax gross receipts representing in part a return of capital, or the power to tax a person who had sustained a net loss, ratification certainly would have failed. See Congressional Record, Volume 44, pages 1533 to 1542, 1558 to 1566, 1568 to 1570, 3377, 3900, 4067, 4105 to 4121, 4389 to 4441 and Volume 45, pages 1694 to 1699, 2245 to 2247, and 2539 to 2540. Never once was it stated that the power sought involved the taxation of gross receipts or *gross* income as distinguished from *net* income. Never once was it suggested that deductions to arrive at the income that could be taxed would be a matter of "legislative grace".

It is not to be supposed that the amendment sought under these circumstances contemplated a surrender by the people to the Federal Government of the power to enact a scheme of taxation fashioned along unfamiliar lines or lines undisclosed during the discussion of the joint resolution. *Burnet* v. *Sanford & Brooks Co., supra*. The only publicly disclosed purpose was limited to the power to impose a tax upon the substantial equivalant of net income in an economic sense, computed upon the basis *of the net result of all* transactions within *the year*. This single purpose guided Senator Brown in the drafting and redrafting of the resolution. This purpose was before both houses of Congress when the resolution was adopted and was certainly known by the legislatures of the several states which ultimately voted its ratification as an amendment to the Constitution.

As to the effect upon the construction of an amendment to a Constitution in the light of the history of the circumstances attending its drafting and adopting, see *Loring* v. *Young*, 239 Mass. 349, 132 N. E. 65; also, *Pollock* case, 158 U. S. 601, 619.

The presumption therefore is clear that the power of taxation sought to be so delegated to Congress was to be fashioned after the scheme of taxation which had been in actual operation within the United States before the amend-

ment. The single purpose was to constitutionally legalize that same scheme of taxation which had been the "familiar practice" before the amendment. That scheme involved the imposition of a tax upon the substantial equivalent of net income in an economic sense, computed upon the basis of the net result of all transactions within the year and recognized losses sustained in trade.

It is not to be assumed loosely that any different (and hence greater) power was intended to be delegated than what was familiar, what was known and what was disclosed as the purpose. This precise thought was expressed by this court in *Burnet* v. *Sanford Brooks Co.*, 282 U. S. 359, when the court said at page 365:

> "The computation of income annually as the *net result* of *all transactions within the year* was a familiar practice, and taxes upon income so arrived at were not unknown, before the Sixteenth Amendment, (Bowers v. Kerbaugh-Empire Co., *supra*, page 174 of 271 U. S., 46 S. Ct. 449; Pacific Insurance Co. v. Soule, 7 Wall. 433, 19 L. Ed. 95; Pollock v. Farmers' Loan & Trust Co., 158 U. S. 601, 630, 15 S. Ct. 912, 39 L. Ed. 1105.) It is not to be supposed that the amendment did not contemplate that Congress might make income so ascertained the basis of a scheme of taxation such as had been in actual operation within the United States before it adoption." (Emphasis ours.)

The power to impose a gross receipts or *gross* income tax is so fundamentally different—greater—more confiscatory unfair, unjust and inequitable than the power to impose a mere *net* income tax, that it is unthinkable that the approval of the request for a power to impose the lesser tax should, (without some clear and definite expression of intention to authorize such a tax) result in the delegation of power to impose the greater, unfamiliar and undisclosed plan of taxation.

The "difference" between a gross receipts tax and a net income tax is "manifest and substantial". The former is a

capital tax, because it applies without reference to "ability to pay". See the discussion of this difference in *United States Glue Company* v. *Town of Oak Creek* 247 U. S. 321, 328, quoted on page 53 of this brief. The latter possesses the *equitable* quality of being payable out of income without impairing capital. This latter quality was stressed in the Congressional debates in defense of the proposed amendment.

The foregoing argument is even more strongly applicable because of the fact that the amendment is in derogation of a fundamental requisition of the original Constitution, "a fundamental requisition deemed so important as to be enforced by two provisions, one affirmative and one negative" (namely, Article I, Section 2, Clause 3, Article I, Section 9, Clause 4). *Pollock* v. *Farmers' Loan & Trust Co.*, 158 U. S. 601, 628, 55 S. Ct. 912, 917.

In construing an amendment to the Constitution, the Court should keep in view the Constitution as it was before it was amended, the purpose to be sought by the Amendment and the specific terms thereof. *Farrell* v. *Keel*, 105 Ark. 380, 161 S. W. 269.

Having in mind that the Sixteenth Amendment, insofar as it is applicable at all, is definitely inconsistent with and in derogation of the two specific provisions of the Constitution referred to above, the meaning of the word "incomes" as used in the Amendment may not be extended by implication beyond the purpose publicly understood in the proceeding on the resolution which resulted in the Amendment. Fundamental rights of the people are not to be deemed surrendered by mere implication. Therefore, "this Amendment shall not be extended by loose construction, so as to repeal or modify, except as applied to income, those provisions of the Constitution that require an apportionment according to population for direct taxes upon property, real and personal". *Eisner* v. *Macomber*, 252 U. S. 189, 206.

The repeal of constitutional provisions by implication is not favored and an amendment should not be construed as affecting any greater innovation of the existing Constitution than is reasonably *necessary* to accomplish the purpose of its enactment. (12 C. J. page 710.)

> "Words or terms used in a constitution which is dependent upon a ratification by the people, must be interpreted in a sense most obvious to the common understanding at the time of its adoption." *State* v. *Butler*, 70 Fla. 102, 133, 69 S. 771.
>
> "Constitutions being the result of a popular will, the words used therein are to be understood ordinarily in the sense that such words convey to the popular mind." *State* v. *Lister*, 91 Wash. 9, 14, 156 P. 858. See also *Prigg* v. *Pennsylvania*, 16 Pet. (U. S.) 539, 610, 10 L. Ed. 1060.

At the time of the ratification of the Sixteenth Amendment the sense in which the word "incomes" was most obvious to the common understanding and the sense in which that word was conveyed to the popular mind was in the sense of net income, profit or gain "upon the *net* result of *all* transactions within the year," (*Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, 365) like the subject matter of the 1894 Act. A gross receipts tax was not being considered. It was not intended.

In construing the meaning of the word "income" as used in Section 38 of the Act of August 5, 1909 (36 Stat. 112) passed before the adoption of the Sixteenth Amendment, this court in *Stratton's Independence* v. *Howbert*, 231 U. S. 399, 415, 34 S. Ct. 136, 140, in defining the word "income" said:

> "* * * 'income' may be defined as the gain derived from capital, from labor, or from both combined, * * *."

This first broad definition of the word "income", was repeated by this court in *Doyle* v. *Mitchell Brothers Company*, 247 U. S. 179, 185, 38 S. Ct. 467, 469 and again in

Eisner v. *Macomber,* 252 U. S. 189, 207, 40 S. Ct. 189, 193, this court in applying this *identical definition* of "income" to the word "incomes" as used in the *Sixteenth Amendment to the Constitution, added* immediately after the exact quotation of the above definition from *Stratton's Independence* v. *Howbert (supra)* and *Doyle* v. *Mitchell Brothers Company (supra)* the language:

> "provided it be understood to include profit gained through a sale or conversion of capital assets to which it was applied in the Doyle Case, * * *."

This court's complete definition of the word thereafter has been repeatedly stated as follows:

> "After full consideration, this Court declared that income may be defined as gain derived from capital, from labor, or from both combined including profit gained through sale or conversion of capital." *Bowers* v. *Kerbaugh-Empire Company,* 271 U. S. 170, 174, 46 S. Ct. 449, 451.

Thus in order to determine whether the *combined* uses of *all* of respondent's labors and capital resulting from *all* transactions within the year 1932 resulted in "gain" or "income" so as to be subject to tax without apportionment, none of the activities or uses of his capital or labor or both combined may be arbitrarily ignored without doing violence to "incomes" in the constitutional sense intended by the Sixteenth Amendment.

The provisions of section 23 (r) of the Revenue Act of 1932 necessarily require that substantial uses to which respondent put his capital and labor be ignored for the purpose of fixing the subject matter of the tax, with the result that, although his uses of his capital and his labors for the year resulted, not in income, but in a *loss* of more than \$145,000.00, the statute taxes that loss as though it were income. Our challenge, however only goes so far as the Commission in the amount of \$7,493.50 are regarded by this Court as disallowed by the statute.

An unapportioned tax on such a substantial loss is a tax upon gross receipts representing a return of capital. It is thus a direct tax on that capital and being unapportioned is therefore void under the prohibition of Article I, Section 2, Clause 3 and Section 9, Clause 4 of the Constitution.

In *Bowers* v. *Kerbaugh-Empire Co.* (*supra*), the defendant in error had borrowed from 1911 to 1913 from a bank and loaned to its subsidiary approximately two million dollars in United States currency giving therefor its notes which it paid off in 1921 with depreciated German marks purchased for a comparatively small amount in United States currency. The money so borrowed had been advanced to its subsidiary for certain construction work which resulted in a total loss and no part of the advances were ever recovered by the defendant in error from its subsidiary. The Government contended that the difference between the amount actually borrowed and the actual cost of its repayment in United States currency was income in the constitutional sense, arguing that the Supreme Court should look only at that portion of the entire series of transactions there which involved gain, that it should ignore that portion of the transactions which involved the use of the gain to recoup its losses previously sustained and that it should ignore the fact that the entire series of transactions resulted in a loss.

The Supreme Court refused to ignore any part of the entire transaction and after emphasizing the required limitation under the Sixteenth Amendment to "put on the same basis all 'incomes' from whatever source derived" said: (271 U. S. 170, 174)

> "In determining what constitutes income substance rather than form is to be given controlling weight. *Eisner* v. *Macomber*, *supra*, (40 S. Ct. 189).
>
> "The transaction herein question did not result in gain from capital and labor, or from either of them, or in profit gained through the sale or conversion of cap-

ital. The essential facts set forth in the complaint are the loans in 1911, 1912, and 1913, the loss in 1913 to 1918 of the moneys borrowed, the excess of such losses over income by more than the item here in controversy, and payment in the equivalent of marks greatly depreciated in value. *The result of the whole transaction was a loss.*" (emphasis ours).

In the above decision the Supreme Court did not call the "cash gain" there statutory "gross income" and justify the elimination of the tax on the theory of some specific *statutory* deduction. After pointing out that "income" in the Constitution means the same as "income" under the 1909 Act, it specifically justified its conclusion on the view that "income" in the constitutional sense must be "income" in "substance" as determined by "the result of the whole transaction".

Although the statute provided no specific deduction to create the offset, the Court found in effect that "income" in the constitutional sense *implies* an offsetting of losses against gains that looks to the "substance" or the net "result of the whole transaction". In other words, if the statute does not specify the deduction necessary to result in the taxation of *NET INCOME IN A SUBSTANTIAL ECONOMIC SENSE* the Constitution will require such an offset or deduction by implication to bring about that result.

On page 17 of petitioner's brief it is argued "that deductions are a matter of legislative grace, *New Colonial Ice Co. v. Helvering*, 292 U. S. 435, 440". This thought suggests the view which has been sometimes adopted that these same contentions were rejected in the case of *Brushaber* v. *Union Pacific Railroad Co.*, 240 U. S. 1, 36 S. Ct. 236, and in the case of *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, 36 S. Ct. 278.

Let us review this thought further. The case of *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 158 U. S. 601, was authority before the Sixteenth Amendment for the view that the character of a tax on an income as direct or

indirect in the constitutional sense was to be determined by the nature of the property which was the source of the income and that, a tax on the income from real or personal property was in substance a tax on the property itself. Therefore because a tax on the property would be a direct tax, a tax on the income would thus also be a direct tax and void for want of apportionment.

As stated more recently by this Court in *National Life Insurance Co.* v. *United States,* 277 U. S. 508, 521, 48 S. Ct. 591, 593:

> "It is settled doctrine that directly to tax the income from securities amounts to taxation of securities themselves, Northwestern Mutual Life Ins., Co. v. Wisconsin, 275 U. S. 136, 48 S. Ct. 5, 72 L. Ed. 202 (November 21, 1927)."

After the Amendment, in *Brushaber* v. *Union Pacific Railroad Co., supra,* and *Stanton* v. *Baltic Mining Co., supra,* it was contended that 1913 income tax was unconstitutional, among other things, because the amendment authorized only a particular character of direct tax without apportionment, and, therefore, if a tax is levied under its assumed authority which does not partake of the characteristics exacted by the amendment, it is outside the amendment and is void as a direct tax in the general constitutional sense, because it is not apportioned. This Court in rejecting this contention also clearly repudiated its former reasoning in the *Pollock* case by which it had reached the conclusion that a tax upon income was not an excise but was equivalent to a tax on the property itself and, hence, a direct tax. In rejecting this former theory, this Court termed it "a mistaken theory deduced from the origin or source of the income taxed." *Stanton* v. *Baltic Mining Co., supra,* 240 U. S. 103, 113, 114, 36 S. Ct. 278, 281.

Mr. Chief Justice White in rendering the opinion of the Court said at the same point, that independently of the effect of the Sixteenth Amendment, an income tax on the

product of a mine, like the corporation excise tax, which levied a tax on doing business and measured it by income, was "not a tax upon property as such because of its ownership, but a true excise levied on the results of the business of carrying on mining operations." But his reasoning in rendering the opinions of the Court in neither the *Brushaber* case, *supra*, nor the *Baltic Mining Co.* case, *supra*, squarely met or disposed specifically of the thought that if the thing sought to be taxed without apportionment was not *income* in the constitutional sense, but was to any extent property, to that extent a tax thereon would be a direct tax and void for want of apportionment. His reasoning instead criticized the argument along with all the other contentions of the taxpayers on the ground that if acceded to the argument would cause one provision of the Constitution to destroy the other, and further, that the tax authorized under the amendment being direct would come neither under the uniformity nor apportionment rules thus giving power to impose unequal taxes in different states.

He also stated:

> "There is no escape from the conclusion that the amendment was drawn for the purpose of doing away for the future with the principle upon which the Pollock case was decided; that is, of determining whether a tax on income was direct not by a consideration of the burden placed on the taxed income upon which it directly operated, but by taking into view the burden which resulted on the property from which the income was derived, since in express terms the Amendment provides that income taxes, from whatever source the income may be derived, shall not be subject to the regulation of apportionment." *Brushaber* v. *Union Pacific Railroad Co.*, 240 U. S. 1, 18, 36 S. Ct. Rep. 238, 241, 242.

In *Eisner* v. *Macomber*, 252 U. S. 189, 205, 206, 40 S. Ct. 189, 192, 193, Congress had sought to tax stock dividends without apportionment under the supposed authority of the

Sixteenth Amendment as though stock dividends in reality constituted income in the sense used in the Amendment. The issue there as in the *Brushaber* case and *Baltic Mining Co.* case, was whether by virtue of the Sixteenth Amendment Congress has the power to tax as income and without apportionment something (a stock dividend) received by the taxpayer which is not "income" in the sense of the Amendment. The receipts sought to be taxed in the *Brushaber* and *Baltic Mining Co.* cases constituted receipts representing in substantial part a return of capital.

It is believed that if the broad observations and reasoning applied by this court in the *Brushaber* and *Baltic Mining Co.* cases, *supra*, had been followed, the similar contention raised by the taxpayer in the *Macomber* case would have been rejected. However, this court in the *Macomber* case clearly adopted reasoning which it had broadly rejected in the *Brushaber* and *Baltic Mining Co.* cases and also reaffirmed its view in the *Pollock* decisions to the extent not affected by the Amendment. It held in effect that its decision there was only affected by the Amendment to the extent that the thing sought to be taxed was *income*. This court said in the *Macomber* case, *supra* (252 U. S. 189, 205):

> "The Sixteenth Amendment must be construed in connection with the taxing clauses of the original Constitution and the effect attributed to them before the Amendment was adopted. * * *
>
> "A proper regard for its genesis, as well as its very clear language, requires also that this Amendment shall not be extended by loose construction, so as to repeal or modify, except as applied to income, those provisions of the Constitution that require an apportionment according to population for direct taxes upon property, real and personal. This limitation still has an appropriate and important function, and is not to be overridden by Congress or disregarded by the courts.
>
> "In order, therefore, that the clauses cited from article 1 of the Constitution may have proper force and effect, save only as modified by the amendment, and that the latter also may have proper effect, it becomes

> essential to distinguish between what is and what is not 'income', as the term is there used, and to apply the distinction, as cases arise, according to truth and substance, without regard to form. Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised."

Thus did this court clearly and emphatically adopt as its views contentions which it had rejected along with others in the *Brushaber* and *Baltic Mining Co.* cases, *supra.*

So long as the deductions allowed result "in computing incomes" not substantially greater than the economic income of the year as the result of *all* the *transactions*, such deductions are matters of clear constitutional right. But as to deductions exceeding those necessary to produce the equivalent of economic income within the year from *all transactions*, such deductions are clearly matters of "legislative grace". An example of such deductions is the deduction "for losses suffered in an earlier year" as in the case of *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435, 54 S. Ct. 788. Such deductions place a tax on less income than the taxpayer had and do not result in taxing something which exceeds income in the constitutional sense. Further illustrations of allowances which are matters of "legislative grace" are personal exemptions, contributions, casualty losses in no way related to income and other allowances amounting to a privilege having no relation to income in the economic sense. Naturally, all the ordinary and necessary expenses incurred in getting the so-called gross income are of the kind to which taxpayers are entitled as a matter of constitutional right.

This court rejected the "legislative grace" theory of deductions in *National Life Insurance Co.* v. *United States*, 277 U. S. 508, 520, with the following words:

> "The suggestion that, as Congress may or may not grant deductions from gross income at pleasure, it can

deny to one and give to another, is specious, but unsound."

It must be recognized that in computing net income a formula must be used which will be composed of some elements not susceptible of exact computation without prohibitive and burdensome cost. Deductions for depreciation and depletion represent two such elements. Practical substantial accuracy in reflecting these elements as an offset to gross income is all that is necessary. Exact accuracy is probably impossible. Failure of the taxing act to use a formula made up of *exact* elements in all respects does not result in taxing something other than constitutional income. Nor does the inclusion in income, by such a formula, of items of adjustment intended to produce a more substantial equivalent of net income in an economic sense take the resulting subject matter out of the category of the income intended by the Constitution. Thus, in the case of *Helvering* v. *Independent Life Insurance Company*, 292 U. S. 371, the addition to income, for this purpose, of the adjustment of 4 per cent of the book value of real estate owned and occupied has the effect only of producing something more nearly approximating the equivalent of net income in an economic sense.

In all the cases where this court has broadly stated or implied that deductions are a matter of "legislative grace" since its decision in *Eisner* v. *Macomber*, *supra*, the deductions claimed were of the character which were not necessarily allowable in order to arrive at the substantial equivalent of economic income computed as the net result of all transactions within the year. Any apparent expression to the contrary in such cases which might have been included in the language of this court in any one of the cases is merely *obiter dictum* and was not necessary to the conclusion reached by the court in the case.

The words "*obiter dictum*" mean a remark by the way. Such an expression constituting "*obiter dictum*", while en-

titled to respectful consideration as expressing the view of the judge by whom it was uttered, is not binding as authority within the *stare decisis* rule. In *Humphrey's Executor* v. *United States*, 295 U. S. 602, 626, 55 Supreme Court 869, 873, a portion of the opinion of Chief Justice Marshall in *Cohens* v. *Virginia*, 6 Wheat. 264, 399 was quoted as follows:

> "It is a maxim, not to be disregarded, that general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit, when the very point is presented for decision. The reason of this maxim is obvious. The question actually before the court is investigated with care, and considered in its full extent. Other principles which may serve to illustrate it, are considered in their relation to the case decided, but their possible bearing on all other cases is seldom completely investigated."

If the dictum in *Helvering* v. *Independent Life Insurance Company*, *supra*, were to be applied to its fullest extent we believe, it would have the effect of nullifying what this court said in *Eisner* v. *Macomber*, 253 U. S. 189, 206 about defining income so as to circumvent the Constitution.

The thought suggested in the *Brushaber* case, *supra* (pp. 40-41 of this brief) that the 1913 Act taxing income was merely an excise tax and could be justified without reference to the Sixteenth Amendment, regardless of whether the tax was levied in the form of an excise (a tax on "doing business" *measured* by income) or in the form of a direct tax on income itself, is inconsistent with the theory of the *Pollock* case, *supra*, from which this court departed in the *Brushaber* case, but to which it returned again, we believe, in the case of *Eisner* v. *Macomber*, *supra*. The Revenue Act of 1932 is in the form of a direct tax upon what is supposed to be income. In this regard it is in the same form as were the Acts of 1894 and 1916. The form taken by

these three acts is that of a direct tax upon the subject matter of income as distinguished from the form of an excise on doing business *measured* by income, as in the case of the 1909 corporation excise tax law. Thus, if by virtue of Section 23 (r) (1) the Revenue Act of 1932 imposes a tax on receipts, this is in form a direct tax on the receipts themselves and is not in the form of an excise upon the act of receiving. In any event, however, a constitutional limitation may not be refined away by finespun distinctions which result in permitting by an indirect process the doing of substantially the same thing which is prohibited to be done directly.—*Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 581, 15 S. Ct. 673, 689; *Brown* v. *Maryland*, 12 Wheat. 419, 444; *Cook* v. *Pennsylvania*, 97 U. S. 566.

In *Brown* v. *Maryland*, *supra*, Chief Justice Marshall in delivering the opinion of the court said at page 444 of 12 Wheat.:

> "But if it should be proved that a duty on the article itself would be repugnant to the constitution, it is still argued that this is not a tax upon the article, but on the person. The state, it is said, may tax occupations, and this is nothing more.
>
> "It is impossible to conceal from ourselves that this is varying the form, without varying the substance. It is treating a prohibition which is general, as if it were confined to a particular mode of doing the forbidden thing. All must perceive that a tax on the sale of an article imported only for sale, is a tax on the article itself."

Again, as late as 1935, this court said in *Stewart Dry Goods Co.* v. *Lewis*, 294 U. S. 550, 556, 55 S. Ct. 525, 528:

> "In connection with other provisions of the fundamental law, this court has had occasion to analyze similar acts. In Brown v. Maryland, 12 Wheat. 419, 6 L. Ed. 678, a tax on the occupation of an importer was held a tax on imports obnoxious to the commerce clause. Said the court (page 444 of 12 Wheat.): 'It is impossible to conceal from ourselves, that this is varying the

form, without varying the substance. * * * All must perceive, that a tax on the sale of an article, imported only for sale, is a tax on the article itself.' In Cook v. Pennsylvania, 97 U. S. 566, 24 L. Ed. 1015, a tax on the amount of an auctioneer's sales was declared a tax on the goods sold. In Crew Levick Co. v. Pennsylvania, 245 U. S. 292, 38 S. Ct. 126, 62 L. Ed. 295, a state tax on the business of selling goods in foreign commerce, measured by gross receipts from goods so sold and shipped, was pronounced an impost upon exports."

Therefore, this court, in *Eisner v. Macomber*, *supra*, for example, did not approve of the 1916 tax on stock dividends as being an excise upon the act of receiving them, but it declared the Act unconstitutional as a direct tax prohibited by Article I of the Constitution and beyond the subject matter sought to be excepted from Article I by the Sixteenth Amendment.

One of the reasons which prompted Congress to include in the 1932 Act the provisions of Section 23 (r) (1) was:

"Many taxpayers have been completely or partially eliminating from tax and income some salaries, dividends, returns, etc., by deducting therefrom losses sustained in the stock and bond markets, with serious effect upon the revenue." (See report of the House Ways and Means Committee, page 12, and Senate Finance Committee, page 17, on the 1932 Revenue Bill)

In times of depression the national income will not produce the revenue that it will in times of prosperity. Thus, in times of depression the revenue must be augmented either by increasing the rate of tax or by imposing other taxes which are within the power of Congress. But in such times when an income tax has proved an unsatisfactory revenue producer, it is not proper for Congress to augment the revenue by a tax in the guise of a tax on income by defining income so as to levy a tax on something which is not income. If, for example, a taxing authority has the constitutional power to levy a direct tax on apples, but not on

other fruit, and finds the apple crop in a particular year grossly inadequate to take care of its revenue requirements for which this tax had normally been used it would not be within the Constitutional power of that taxing authority to define apples so as to include lemons for the purpose of augmenting its otherwise insufficient revenue under the law.

This, we believe, is just what Congress did in the 1932 law. Instead, it should have raised the tax rate, sought additional power by the constitutional amendment procedure, or levied other taxes within its power.

We therefore contend that the 1932 Revenue Act cannot be so construed as to disallow the commissions of $7493.50 without rendering the Act unconstitutional to that extent.

V.

To the extent that the limitation provisions of Section 23(r) and (t) of the Revenue Act of 1932 may be construed by this Court as disallowing the buying commission in the amount of $7,493.50, such provisions are unconstitutional and therefore void under the Due Process clause of the Fifth Amendment to the Constitution because they create arbitrary, whimsical, and capricious discrimination against persons whose activities consist in part or in whole of buying and selling securities for profit.

This contention is made by respondent solely in the alternative and as in the previous point only in support of the judgment below allowing the deduction for buying commissions in the amount of $7493.50. This argument does not seek to attack the judgment below.

While it is not within the scope of the Fifth Amendment nor the Fourteenth Amendment to withhold the power of classification, if the law deals alike with all of the certain class, yet it is equally true that such classification cannot be made arbitrarily. In *Gulf C. & S. F. Ry. Co.* v. *Ellis*, 165 U. S. 150, 17 S. Ct. 255 this court said:

> "The state may not say that all white men shall be subjected to the payment of the attorney's fees of parties successfully suing them, and all black men not. It may not say that all men beyond a certain age shall be alone thus subjected, nor all men possessed of a certain wealth. These are distinctions which do not furnish any proper basis for the attempted classification. That must always rest upon some difference which bears a reasonable and just relation to the act in respect to which the classification is proposed, and can never be made arbitrarily, and without any such basis."

Again in *Connelly* v. *Union Sewer-Pipe Company*, 184 U. S. 540, 22 S. Ct. 431 this court said with regard to arbitrary classification:

"* * * This court has held that classification 'must always rest upon some difference which bears a reasonable and just relation to the act in respect to which the classification is proposed, and can never be made arbitrarily, and without any such basis * * * but arbitrary selection can never be justified by calling it classification.'"

A classification which favors persons engaged in the sale or exchange of stocks and bonds who happen to be "dealers in securities" as to stocks and bonds "acquired for resale to customers" in respect of transactions in the "ordinary course of business" over persons engaged in the sale or exchange who do not happen to qualify as "dealers in securities" or who do not happen to acquire the stocks and bonds for resale to customers even though such transactions are in the ordinary course of his business, is a purposeless, arbitrary, unreasonable, whimsical, and capricious discrimination in favor of persons in the former class. The distinction between these two classes creates a discrimination of an unusual character previously unknown to the practice of our Government. No sensible reason is apparent for the creation of such a peculiar and unusual differentiation between classes.

If a so-called "dealer" had "other income" equal to respondent's "other income" and had sustained losses on stocks held less than two years equal to respondent's similar losses, the so-called "dealer" would pay no tax. Or if respondent's trading or speculation loss had been in commodities instead of stocks, no tax would have resulted. Respondent's business is trading in stocks. What good reason is there for discriminating against him in favor of a so-called "dealer" or in favor of one whose business is trading in commodities?

As stated by McGeHee at Page 211 of his work "Due Process of Law"

"* * * Clear hostile discrimination against particular persons and classes, especially such as are of an

unusual character, unknown to the practice of our Government, might be obnoxious to the constitutional prohibition."

In *Nebbia* v. *People of State of New York*, 291 U. S. 502, 525, 54 S. Ct. 505, 510, this court said in respect to the meaning of the due process clauses of the Fifth and Fourteenth Amendments to the Constitution,

> "The Fifth Amendment, in the field of federal activity, and the Fourteenth, as respects state action, do not prohibit governmental regulation for the public welfare. They merely condition the exertion of the admitted power, by securing that the end shall be accomplished by methods consistent with due process. And the guaranty of due process, as has often been held, demands only that the law shall not be unreasonable, arbitrary, or capricious, and *that the means selected shall have a real and substantial relation to the object sought to be attained*." (Emphasis ours.)

The purpose of a revenue law must be solely to collect revenue and not to discourage certain kinds of honest business activity. Such purposes not germane to the collection of the Revenue are arbitrary and if they are discriminatory without a reasonable and *just* relation to the matter of collecting revenue, or they become unjust and unreasonable and offensive to the Constitution.

That a Federal taxing statute may be so arbitrary and whimsical as to violate the "Due Process" provisions of the Fifth Amendment to the Constitution has been definitely determined by this court. In *Nichols* v. *Coolidge*, 274 U. S. 531, 542, 47 S. Ct. 710, 714, this court said as to "the arbitrary, whimsical, and burdensome character of the challenged tax" that:

> "This Court has recognized that a statute proporting to tax may be so arbitrary and capricious as to amount to confiscation and offend the Fifth Amendment. Brushaber v. Union Pacific R. R., 240 U. S. 1, 24, 36 S. Ct. 236, 60 L. Ed. 493, L. R. A. 1917B, 414, Ann. Cas.

1917B, 713; Barclay & Co. v. Edwards, 267 U. S. 442, 450, 45 S. Ct. 135, 348, 69 L. Ed. 703. See, also, Knowlton v. Moore, 178 U. S. 41, 77, 20 S. Ct. 747, 44 L. Ed. 969."

This court has since invoked this same principle in the following cases: *Helvering* v. *Helmholz*, 296 U. S. 93, 56 S. Ct. 68, 70; *Hassett* v. *Welch*, 303 U. S. 303, 311, 58 S. Ct. 559, 563; *Heiner* v. *Donnan*, 285 U. S. 312, 326.

Thus it is now clear that the prohibition against the Federal Congress in the Fifth Amendment to the Constitution that "no person shall * * * be deprived of * * * property, without due process of law * * *" is a limitation upon the taxing power of the Federal Congress and that arbitrary, whimsical, or capricious classifications or discriminations which result in the imposition of greater burden under one such classification than under another are void as repugnant to the said Fifth Amendment to the Constitution.

An example of the discriminatory effect of this capricious limitation is that persons engaged in buying and selling futures in the Chicago Grain Exchange may deduct their losses from such transactions from their other income while persons engaged in buying and selling securities on the New York Stock Exchange may not so deduct their losses from such transactions from their other income.

Why one method of speculation should be favored at the expense of another does not appear. The discrimination is wholly without substantial reason, *it rests upon no difference which bears a reasonable and just relation to the act in respect to which the classification is proposed*, and therefore renders the limitation provisions of Sections 23(r) and (t) of the Revenue Act of 1932 clearly arbitrary, whimsical, and capricious. The limitation is thus void as violative of the provisions of the Fifth Amendment of the Constitution.

Furthermore, the provisions of Section 23(r)(1) have the effect of applying the progressive rates of income tax

without relation to the taxpayer's "ability to pay." This circumstance destroys the reasonable basis for the discrimination otherwise inherent in the progressive income tax rate schedule. The only constitutional justification for the discrimination arising from the application of a graduated scale of rates in income taxation is the superior ability to pay of those upon whom the higher rates are imposed. Graduated rates must bear a reasonable relation to the current *increase* in net worth of the taxpayer resulting from transactions completed during the taxable year.

Losses of a taxpayer which occur in his trade or business reduce his net worth. Such losses must, therefore, be taken into account in applying a schedule of graduated rates based on ability to pay. Mr. Winmill had an actual loss of $145,000 during the taxable year, yet under the statute he must pay a normal tax on $35,000 and a graduated surtax on $52,000 although he actually sustained the large net loss.

The general principles governing this phase of the case were clearly stated by the Supreme Court in the case of *Stewart Dry Goods Co.* v. *Lewis,* 294 U. S. 550, 558, in which the Court said:

> "The district court found that 'generally speaking' he who sells more is in receipt of a greater profit and hence has larger ability to pay, and upon this basis justified the classification. But it is to be remembered that the act in question taxes gross sales and not net income. As stated in *United States Glue Co.* v. *Town of Oak Creek,* 247 U. S. 321, 328:
>
> " 'The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference

between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large.'

* * * * *

"The proofs submitted are insufficient to support the appellees' contention that the graduation of the tax was adjusted with reasonable approximation to the net earnings of the taxpayers.

* * * * *

"An income levy by its very nature assures equality of treatment, because the burden of the exaction varies with increase or decrease of return on capital invested and with the comparative success or failure of the enterprise.

* * * * *

"As we have said, the statute does not purport to levy a tax on incomes. Plainly it does not in fact do so. A merchant having a gross business of $1,000,000, but a net loss, must pay a greater tax than one who has a gross of $400,000 and realizes a substantial net profit.

* * * * *

"The law arbitrarily classifies these vendors for the imposition of a varying rate of taxation, solely by reference to the volume of their transactions, disregarding the absence of any reasonable relation between the chosen criterion of classification and the privilege, the enjoyment of which is said to be the subject taxed. It exacts from two persons different amounts for the privilege of doing exactly similar acts because the one has performed the act oftener than the other.

"We hold the act unconstitutional."

In *Heiner* v. *Donnan*, 285 U. S. 312, 327, 52 S. Ct. 358, 361, Congress levied a tax on transfers at death and to prevent its avoidance had imposed a tax which purported to be in the guise or name of a tax on a transfer in contemplation of death. Although it had the right to tax any transfer, it created a conclusive presumption, irrespective

of true fact, that transfers made less than two years prior to death were made in contemplation of death. This court held that presumption void as violative of the Fifth Amendment and likened such tax to a tax on one person based on another's property. In describing the effect of burdening one taxpayer with a tax measured in part by property belonging to another, this court said:

> "Plainly, this is to measure the tax on A's property by imputing to it in part the value of the property of B, a result which both the Schlesinger and Hoeper Cases condemn as arbitrary and a denial of due process of law. Such an exaction is not taxation but spoliation. 'It is not taxation that government should take from one the profits and gains of another. That is taxation which compels one to pay for the support of the government from his own gains and of his own property.' United States v. Baltimore & Ohio R. Co., 17 Wall. 322, 326, 21 L. Ed. 507."

It is just as wrong to levy a tax in the name or guise of an income tax, which taxes only one's *successful* transactions during the year and ignores his unsuccessful ones, as it is to tax one person on another's income. In neither event is he being taxed on income which in true fact he enjoyed. The transactions resulting in losses have the effect of absorbing or turning into actual losses during the year the taxpayer's gains for the same period, thus impairing his ability to pay. Thus, while the Act professes to tax what in fact is income, Section 23 (r) (1) thereof creates a *conclusive presumption contrary to actual fact*, which results in taxing something which is not income.

The very illustration (used by this court in *Heiner* v. *Donnan, supra*), of a conclusive presumption contrary to fact, which could offend the due process clause of the Constitution, exactly fits the situation here, and we believe the imposition of such a tax is prohibited by the Constitution. In that case this court said at page 326 of 285 U. S., 52 S. Ct. 358, 361:

"That which is not in fact a taxpayer's income cannot be made such by calling it income."

CONCLUSION.

In view of the matters hereinbefore discussed, it is respectfully prayed that the judgment of the United States Circuit Court of Appeals below, allowing buying commissions as a deduction from income, be affirmed.

Respectfully submitted,

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FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

No. 11.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

ROBERT C. WINMILL, *Respondent*.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

SUPPLEMENTAL BRIEF FOR THE RESPONDENT.

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CASES CITED.

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ARGUMENT.

IV.

To the extent that Section 23 (r) of the Revenue Act of 1932 may be held by this court to disallow the buying commissions in the amount of $7,493.50, such Section is unconstitutional and void under Article I, Section 2, Clause 3 and Section 9, Clause 4 of the Constitution, because as so construed the Act levies a direct unapportioned tax on subject matter not contemplated by the word "incomes" within the meaning of the Sixteenth Amendment to the Constitution.

Supplementing respondent's argument set forth on pages 27 to 48, inclusive of his brief, and particularly with reference to the meaning of the word "incomes" as used in the Sixteenth Amendment to the Constitution, the atten-

tion of this court is respectfully called to the decision of the Supreme Judicial Court of Massachusetts in the case of *Trefry, Tax Commissioner* v. *Putnam*, 227 Mass. 521, 524, 116 N. E. 904, 907 (1917). In that case the court had before it the question of the meaning of the word "income" as used in the Forty-fourth Amendment to the Constitution of Massachusetts. The court said:

> "'Income', like most other words, has different meanings dependent upon the connection in which it is used, and the result intended to be accomplished. * * * In its ordinary and popular meaning, 'income' is the amount of actual wealth which comes to a person during a given period of time. At any single moment a person scarcely can be said to have income. * * * It is common speech for one to say that he made so much money during a particular 12 months and to mean thereby that he has increased his wealth to that amount."

The court in its opinion referred to the meaning of the word "incomes" as used in the then recent Federal statutes and decisions of the Federal courts, including the 1913 law, which was passed under the Sixteenth Amendment to the United States Constitution, authorizing a tax only on "incomes." These Federal references to "incomes," the court stressed, may be presumed to have been familiar to the members of the general court and the people, during the discussion accompanying the adoption of the Forty-fourth Amendment, and also that the interpretation of the word "incomes," as adopted by the Federal statutes "is matter of common knowledge." The court pointed further to the decisions under the Federal income tax law and limited the word "incomes" to that which during the year "was received and converted into cash" as distinguished from that which "would be known in common speech as mere paper profits."

On the basis of these reasons, briefly summarized above, the court reached the conclusion as to the meaning of the word "income" that:

"* * * the tax upon gains in excess of losses arising from sales of stock during the year 1916 is a tax upon income * * *."

From the foregoing it is clear that the word "income", in the sense most obvious to the common understanding at the time of the adoption of the Forty-fourth Amendment to the Massachusetts Constitution, would be identical with the meaning of the word "incomes" as commonly understood by the Congress and the people concerned at the time of the ratification of the Sixteenth Amendment to the Federal Constitution. And the meaning of the word "incomes" in the sense most obvious to the common understanding must have been briefly as follows:

> Income means the increase in one's wealth, arising from the excess, during a stated period of time, of gains from all sources over all losses in trade, with the understanding that the gains and losses must be realized gains and losses as distinguished from mere paper profits or losses.

This concept of income has been followed by the Supreme Judicial Court of Massachusetts in the following cases: *United States Trust Co. et al.* v. *Commissioner of Corporations and Taxation*, 13 N. E. (2d) 6, 8 (1938); *Bryant* v. *Commissioner of Corporations and Taxation*, 197 N. E. 509, 510; *Van Heusen* v. *Commissioner*, 257 Mass. 488, 154 N. E. 257; *Bingham et al.* v. *Long, Tax Commissioner*, 249 Mass. 79, 80; and *Brown* v. *Commissioner of Corporations and Taxation*, 242 Mass. 242, 244, 136 N. E. 188, 189.

In the light of these views, it is clear that the meaning of "income" most obvious to the common understanding, certainly does not contemplate a *net loss* of over a hundred thousand dollars. Therefore, during the year 1932 respondent did not have income in that sense which would produce a tax thereon in excess of a deficiency determined on the basis of the judgment of the court below.

V.

To the extent that the limitation provisions of Section 23 (r) and (t) of the Revenue Act of 1932 may be construed by this court as disallowing the buying commissions in the amount of $7,493.50, such provisions are unconstitutional and therefore void under the Due Process clause of the Fifth Amendment to the Constitution because they create arbitrary, whimsical, and capricious discrimination against persons whose activities consist in part or in whole of buying and selling securities for profit.

Supplementing respondent's argument set forth on pages 49 to 56, inclusive of his brief, particularly with respect to the discriminatory features of the Revenue Act of 1932, the deficiency on the basis of the judgment of the court below may not be increased.

> "In resolving the issue we are not concluded by the name or description of the tax as found in the Act; our duty is to ascertain its nature and effect." *Stewart Dry Goods Company* v. *Lewis*, page 555 of 294 U. S.

By its very nature, the Revenue Act of 1932 is not an income tax act, although its name and description so indicate. The reason for this statement is indicated by a statement of this court in *Stewart Dry Goods Co.* v. *Lewis*, at page 560 of 294 U. S. which is as follows:

> "An income levy by its very nature assures equality of treatment, because the burden of the exaction varies with increase or decrease of return on capital invested and with the comparative success or failure of the enterprise."

This test is not satisfied by the Revenue Act of 1932 insofar as respondent is concerned, because of the fact that although he sustained a substantial loss on his unsuccessful enterprises, under the Act he must pay tax on a substantial gain which was wiped out by the losses.

The important fact must not be lost sight of in this case that the tax imposed upon respondent is a *graduated normal tax and surtax*, as distinguished from the *flat rate corporation tax* which alone was involved in *Helvering* v. *Independent Life Ins. Co.*, 292 U. S. 371, and *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435. The imposition of such *graduated taxes* is a discrimination against those who pay a tax at a higher rate in favor of those who pay a tax at a lesser rate. Such a discrimination it has been held by abundant authority must bear some,

> "reasonable relation between the chosen criterion of classification and the privilege, the enjoyment of which is said to be the subject taxed." *Stewart Dry Goods Co.* v. *Lewis*, 294 U. S. 550.

As pointed out by this court in that case, the doing of exactly similar acts more oftener by one than another is not a reasonable criterion for increasing graduations of classifications.

The inequality may be justified only by the relative ability of persons more greatly discriminated against to pay. This court in the *Stewart Dry Goods Co.* case, *supra*, held the Kentucky graduated gross sales tax to be an arbitrary and capricious discrimination offensive to the Fourteenth Amendment to the Constitution, because among other things one of the petitioners there for one year had a net income of approximately $98,000, without the tax, but would have had a loss of approximately $9,000 after deducting the $107,000 tax demanded under the law. While the tax in the instant case purports to be a *net income tax*, the limitation of losses, provided for in Section 23 (r) (1) changes the "nature and effect" of the tax to a *gross reaeipts tax*.

Specifically, respondent's activities from all sources reflected a loss of approximately $145,000, and yet under the Commissioner's interpretation of the statute he would pay a so-called "income tax" thereupon as though he had a net income of approximately $35,000. The resulting discrimination here and the arbitrary and capricious burden imposed

bears no "reasonable relation between the chosen criterion of classification and the privilege" taxed. Certainly, if the graduated discriminatory tax in the *Stewart Dry Goods* case, *supra,* which was sufficient only "to make the difference between profit and loss," is arbitrary and offensive to the Fourteenth Amendment; an arbitrary discriminatory tax, which has the effect of *increasing a net loss already sustained,* must be even more offensive to the same principles and as such contrary to the due process provisions of the Fifth Amendment to the Constitution, which is a limitation upon the Federal taxing power. If such cases as *Brushaber* v. *Pacific Railway Co.,* 240 U. S. 1, *Stanton* v. *Baltic Mining Co.,* 240 U. S. 103, *Burnet* v. *Thompson Oil & Gas Co.,* 283 U. S. 301, are inconsistent with the *Stewart Dry Goods Co.* case, *supra,* it must be presumed that to the extent of such inconsistency they were overruled by the latter case.

Helvering v. *Independent Life Insurance Co.,* 292 U. S. 371, and *New Colonial Ice Co.* v. *Helvering,* 292 U. S. 435, are in no wise inconsistent with the *Stewart Dry Goods Co.* case, *supra,* because they involve only a non-discriminatory *flat rate corporation tax.* Whereas, the tax on respondent is a tax on an individual and is a discriminatory tax computed on the basis of graduated normal taxes and graduated surtaxes, having no relation to his ability to pay.

Respondent in discussing the similarity of the restraint in the fields of Federal and State action, imposed respectively by the Fifth and Fourteenth Amendments to the Constitution, did not point out that the *Stewart Dry Goods* case, *supra,* was decided by this court with reference to the "equal protection" clause of the Fourteenth Amendment without specific reference to the "due process" clause of that amendment.

It may be desirable, therefore, at this point to suggest what respondent believes to be the analogy indicated by the decisions of this court between the "equal protection" clause of the Fourteenth Amendment on the one hand and the "due process" clauses of the Fifth and Fourteenth Amendments on the other hand. From the cases decided

by this court and cited in respondent's brief (pages 49 to 55 incl.) it appears that the "arbitrary", "capricious" and "whimsical" character of a taxing law will be held offensive either under the equal protection clause of the Fourteenth Amendment or the due process clause of either the Fifth Amendment or the Fourteenth Amendment. No particular degrees of arbitrariness, capriciousness or whimsicality appear to have been defined as applicable to one clause or the other, and the conclusion is irresistible that what would be arbitrarily offensive to one would be arbitrarily offensive to the others. The same may be said of the interchangeable use (with relation to all these clauses) of references to classifications which are offensive because the means selected has no substantial relation between the chosen criterion of classification and the privilege. This, or a similar expression, is used by this court interchangeably with reference to the "equal protection" and the "due process" clauses of the Federal Constitution. That this reasoning is applicable to the Federal taxing power is indicated by such cases as: *Nichols* v. *Coolidge*, 274 U. S. 531; *Helvering* v. *Helmholz*, 296 U. S. 93; *Hassett* v. *Welch*, 303 U. S. 303, and *Heiner* v. *Donnan*, 285 U. S. 312.

While the foregoing discussion may not be necessary, respondent believes that it justifies the application to the Federal taxing power under the "due process" clause of the Fifth Amendment to the Constitution of everything which was said by this court with respect to the "equal protection" clause of the Fourteenth Amendment in the case of *Stewart Dry Goods Company* v. *Lewis*, *supra*.

The imposition of the arbitrary and discriminatory tax in question here may not be increased over the amount computed on the basis of the judgment of the court below. The judgment therefore should be affirmed.

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SUPREME COURT OF THE UNITED STATES.

No. 11.—October Term, 1938.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Robert C. Winmill.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[November 7, 1938.]

Mr. Justice Black delivered the opinion of the Court.

Respondent—in his 1932 income tax return—deducted from his gross income brokerage commissions paid and incurred in purchasing securities during that taxable year. Section 23 (a) of the Revenue Act of 1932 allows as deductions "All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; . . . ." Respondent contends that he was engaged in the "business" of buying and selling securities and that the brokerage commissions amounted to "compensation for personal services actually rendered" within the meaning of Section 23 (a).

The Government insists that brokers' commissions in security purchases are "expenditures, . . . properly chargeable to capital account" constituting "a part of the cost" of such property and serving only to increase respondent's loss from sales of stock under Sections 111 and 23 (r) which control allowable losses on disposal of stocks.[1] Section 23 (r) allows losses on stock sales to be

[1] Revenue Act of 1932, c. 209, 47 Stat. 169, Sec. 111. Determination of Amount of Gain or Loss.

(a) Computation of Gain or Loss.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

Sec. 113. Adjusted Basis for Determining Gain or Loss.

(b) Adjusted Basis.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

deducted only to the extent of gains realized from such sales. If respondent was engaged in the "business" of buying and selling securities, and the brokers' commissions were not a "part of the cost" of the securities purchased, but were ordinary business expenses [as defined in Section 23 (a)], respondent was justified in deducting the brokers' commissions from his gross income for the taxable year. However, if these commissions represent a part of the cost of the securities, respondent's right to deduct is limited by Section 23 (r).

The Commissioner refused to permit the deductions beyond the extent of stock losses. His action was affirmed by the Board of Tax Appeals.[3] The Court of Appeals held the commissions deductible if respondent was engaged in the business of buying and selling securities, and remanded for a finding as to the nature of his business.[4]

Article 282, Treasury Regulation 77, issued under the 1932 Act, provides that "Commissions paid in purchasing securities are a part of the cost price of such securities." If this regulation governs, the respondent's contention cannot be sustained.

Regulations promulgated under the 1916 income tax law treated commissions in security purchases as a part of the securities' cost and not as ordinary expense deductions.[5] This interpretation has consistently reappeared in all regulations under succeeding tax

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(1) General Rule.—Proper adjustment in respect of the property shall in all cases be made—

(A) for expenditures, receipts, losses, or other items, properly chargeable to capital account, including taxes and other carrying charges on unimproved and unproductive real property, but no such adjustment shall be made for taxes or other carrying charges for which deductions have been taken by the taxpayer in determining net income for the taxable year or prior taxable years; . . .

[2] Revenue Act of 1932.

Sec. 23. Deductions from Gross Income. In computing net income there shall be allowed as deductions:

(r) Limitation on Stock Losses.

(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

[3] 35 B. T. A. 804.

[4] 93 F. (2d) 494.

[5] See, Art. 8, Paragraph 108, T. R. 33 (Revised 1918).

statutes.[6] In the period since 1916 statutes have from time to time altered allowable deductions, but it is significant that Congress substantially retained the original taxing provisions on which these regulations have rested.

Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law.[7]

There has been tacit, if not express judicial approval for the administrative treatment of commissions as an element of the cost of securities. In *Hutton* v. *Commissioner*, 39 F. (2d) 459, 460, the Court of Appeals recognized that "It has long been a settled rule of the Treasury Department that commissions paid in purchasing securities are a capital expenditure as part of the cost price of the securities."

In recognition of this administrative regulation, it has been said here that ". . . . commissions [paid for marketing bonds] do not differ from brokerage commissions paid upon the purchase or sale of property. The regulations have consistently treated such commissions, not as items of current expense, but as additions to the cost of property or deductions from the proceeds of sale, in arriving at net capital profit or loss for purposes of computing the tax."[8]

Respondent points to an apparent inconsistency between the general provision in Treasury Regulation 77, Article 121, that "Among the items included in business expenses are . . . commissions," and Article 282 which specifically and particularly declares that "Commissions paid in purchasing securities are a part of the cost price of such securities." Special provisions limit the application of those of a broad and general nature relating to the same subject. The special designation of security purchase commissions as a "part of the cost price of such securities" contained in Article 282 evinces the clear intent to withdraw that special

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[6] Art. 293 of T. R. 45 (1918), 62 (1921); Art. 292 of T. R. 65 (1924), 69 (1926); Art. 282 of T. R. 74 (1928), 77 (1932); Art. 24-2 of T. R. 86 (1934), 94 (1936).

[7] United States v. Dakota Montana Oil Co., 288 U. S. 459, 466; Old Mission Co. v. Helvering, 293 U. S. 289, 293, 294.

[8] Helvering v. Union Pacific Co., 293 U. S. 282, 286.

type of commission from the general classification of Article 282.

Nor can it be inferred that the addition of Section 23 (r) to the 1932 Act indicated any congressional purpose to alter or repeal the long existing administrative interpretation of non-deductible capital expenditures under which brokers' purchase commissions have been uniformly considered as a part of the cost of securities and not as current business expenses. This new statutory restriction of the allowance for losses from sales of stock bears no such relationship to the definition of cost price of securities as to lead to the conclusion that Congress intended to overthrow and abandon a settled practice of determining the elements of cost.

The brokers' purchase commissions here constituted a part of the acquisition cost of the securities involved, and are not allowable to the taxpayer as a deduction from gross income under Section 23 (a) of the Revenue Act of 1932. Congress, in the exercise of its power to deny or limit deductions from gross income,[10] has—by Section 23 (r)—limited this taxpayer's allowable deduction. He has a right to a deduction "only to the extent of . . . gains from . . . sales or exchanges of stocks and bonds" as therein provided. The fact—if it be a fact—that respondent was engaged in the business of buying and selling securities does not entitle him to take a deduction contrary to this provision.

The cause is reversed and remanded to the Court of Appeals for action in harmony with this opinion.

Reversed.

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[9] Similarly, if the specific provisions of Article 282 are valid and have the present effect of law, respondent's contention that the commissions are uncompensated losses within the meaning of the general provisions of Section 23 (e) (1) of the 1932 Act is unavailing.

[10] See, Helvering v. Ind. Life Ins. Co., 292 U. S. 371, 381.